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IN THE

Supreme Court of the United States

NATHAN HAUSMAN, JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u/w of Daniel Buckley, deceased, PETER FUNDARO, HAROLD MALTZ, NORVIN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT, in their own behalf as stockholders of Pantepec Oil Company, C.A., and in behalf of all other such stockholders similarly situated,

Petitioners,

—against—

JOHN W. BUCKLEY, THE CATAWBA CORPORATION and PANTEPEC OIL COMPANY, C.A.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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NATHAN HAUSMAN, JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u/w of Daniel Buckley, deceased, PETER FUNDARO, HAROLD MALTZ, NORVIN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT, in their own behalf as stockholders of Pantepec Oil Company, C.A., and in behalf of all other such stockholders similarly situated,

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners Nathan Hausman, Joseph Applebaum, The Applebaum Foundation, Inc., Alfred N. Barnett, Julie A. Buckley, as remaining trustee u/w of Daniel Buckley, deceased, Peter Fundaro, Harold Maltz, Norvin H. Rieser, Fred Weibert and Regina Weibert and L. H. Luckett pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered on February 13, 1962.

Opinions Below

The opinion of the Court of Appeals, printed in Appendix A, *infra*, has not yet been reported. The opinion

of the District Court dated June 27, 1960 is unreported and is printed at p. 12a of the Appendix to petitioners' brief as appellants in the court below.

Earlier opinions of the District Court, having a bearing on this petition, dated September 9, 1958 and November 26, 1958, are printed at pp. 60a and 63a of said Appendix to petitioners' brief below. The opinion dated September 9, 1958 is reported in 22 FRD 304, and the opinion dated November 26, 1958 is unreported.

Jurisdiction

The judgment of the court below was dated and entered on February 13, 1962. The jurisdiction of this Court is invoked pursuant to Title 28 United States Code §1254(1).

Questions Presented

The questions presented arise from the dismissal of this diversity suit, a minority shareholders' derivative action, on the sole ground that the law of Venezuela, the nation of incorporation, allows only a "majority shareholders' action".

The first question forming the basis for this petition is whether, under the doctrine of *Erie R. Co.* v. *Tompkins*, 304 U. S. 64 (1938), the court below properly found that the New York courts would apply the law of Venezuela in bar of the action, state law being silent on the law to be applied in case of a conflict of laws as to the existence of a remedy for minority shareholders. The answer depends on these subsidiary questions, involving the method and technique of ascertaining state law on a novel issue of vital importance to the rapidly growing body of American investors in shares of corporations chartered in foreign countries:

1. Did the court below fail to follow controlling decisions of this Court in its explicit refusal to function in the manner of a state court of last resort?

2. Did the court below profess to follow a "clearly enunciated state rule"[1] of mechanical referral to the law of the nation of incorporation, where no such rule in fact exists?

3. Did the court below, in selecting Venezuelan law, properly disregard, under New York law, the overwhelming local interest exemplified by the American citizenship of 50,000 of the corporation's shareholders, including plaintiffs, and of the adversary defendants; the corporation's American financing and the long trading of its shares on an American exchange; and the likely commission in the United States of the serious and continuing wrongs complained of?

4. Did the court below properly conclude that New York, a pioneer in the grouping of contacts theory of resolving conflicts of law, would eschew that approach in favor of the doctrine of mechanical referral to the law of the place of incorporation as indicated principally by dicta in old cases long antedating New York's adoption of the contacts theory?

5. Did the court below properly exclude from its "data" in ascertaining state law a new state enactment which completely departs from referral to the law of the place of incorporation with regard to shareholders' suits in behalf of so-called domiciled foreign corporations?

6. Did the court below properly find that New York would not reject Venezuelan law as repugnant to local public policy, notwithstanding that the record shows

[1] Appendix A, *infra*, p. 37.

that Venezuela deliberately throttles minority shareholders and leaves them without any practical remedy against managerial fraud?

7. Did the court below properly find that New York would regard the issue of the maintainability of this action by minority shareholders as one of substance rather than one of procedure to be governed by local law?

The second question forming the basis for the petition is the following:

Does comity require recognition of the code of a foreign nation when so doing will strip American investors of all protection afforded by state and federal decisional and statutory law, and convert a foreign charter into a license for plunder?

Petitioners will also raise the following question if the petition is granted:

Under the law of New York is the Venezuelan law defense available to the adversary defendants; and should the corporation be allowed to assert that defense, in bar of its own recovery, in a pleading interposed by attorneys who also represented one of the adversary defendants and who have a personal interest in the outcome?

Statement of the Case

The suit was commenced on April 18, 1957 in the United States District Court for the Southern District of New York. The basis for federal jurisdiction in the court of first instance was diversity of citizenship (66a, 71a, 74a).[2]

[2] Numerals in parentheses refer to the Appendix to petitioners' brief as appellants in the court below.

Plaintiffs-petitioners are stockholders of defendant-respondent Pantepec Oil Company, C.A., a Venezuelan corporation; and they sue derivatively for its benefit (66a). The other parties are defendants-respondents John W. Buckley and The Catawba Corporation. All the plaintiffs and Buckley are citizens of the United States. Catawba is a Delaware corporation qualified to transact business in New York (30a).

Pantepec is American-financed and American-dominated (26a, 31a, 74a-76a). By virtue of an agreement with a New York depositary made in 1938 (31a), Pantepec's bearer shares, evidenced by "American Depositary Receipts", have long traded on the New York Curb and American Stock Exchanges in New York City (26a). The deposit agreement provides (58a):

> "27. All questions concerning the interpretation, validity and effect of this Agreement or of the certificates hereunder shall be determined according to the laws of the State of New York."

Aided by the deposit agreement, Pantepec's management, which includes defendant-respondent Buckley, regularly solicits proxies, in the manner of American corporations, for shareholders' meetings held in Venezuela (44a, 114a). Meetings are attended by few, if any, shareholders not associated with the long-entrenched management of the corporation (80a).

Pantepec has 3,133,819 shares outstanding with more than 50,000 holders, almost all of whom are American citizens (27a, 80a). Plaintiffs hold some 33,000 shares (2a-4a).

The gist of the complaint before the court below was long continuing extraction of large sums from Pantepec by the dominating Buckley management, mainly through so-

called service contracts with Catawba, a Buckley-owned company (74a-80a).[3] The record (30a) indicates that Catawba's headquarters and the real seat of Pantepec's management, and hence the likely locus of the challenged transactions, were and are in New York City.

The judgment in the court below affirms (so far as appealed from) a judgment of the district court (10a) which, before any trial of or pre-trial inquiry into the facts and matters complained of (5a-6a), dismissed the action upon the sole ground that no such remedy as a minority shareholder's suit is available under the law of Venezuela, the chartering nation (12a-24a).

Under Venezuelan law a corporate claim against directors, officers and third parties is "vested" solely in the stockholders' meeting (188a, 19a). No claim can be prosecuted on the corporation's behalf except at the direction of the meeting (19a-20a). Thus the wrongdoers, if effectively in control of management and, thereby of the shareholders' meetings, as alleged here (74a-80a), can mulct the corporation with impunity (163a-164a, 192a).

Minority shareholders are further frustrated by the requirement that stockholders' complaints be channeled to the meeting through an individual, elected by the stockholders, called the *comisario* (186a, 188a). Only if the complaint is by holders of 10% or more of the outstanding stock does the *comisario* have to report to the meeting the facts complained of, as distinguished from mere receipt of the complaint (188a, 21a-22a). The stockholders' meeting has

[3] I.e., the third of the three counts comprising the third amended complaint (66a-82a). Petitioners did not appeal dismissal of the first count (12a), and their main brief in the court below (pp. 15-16) expressly limited their second count appeal to those certain allegations thereof whose dismissal might be deemed dispositive of a particular claim asserted in the third count (viz., paragraph 43 (77a-78a)).

the final say and is the last resort, the only appeal being to another stockholders' meeting (162a).[1] Stockholders' meetings must be held in Venezuela (165a).

Mustering the holders of 10% of stock necessary to have the facts of a complaint placed before a stockholders' meeting is practically foreclosed by other oppressive features of Venezuelan law. Complaining holders must physically deposit their shares with the *comisario* or his designee until the meeting is held (189a, 156a-157a). Moreover, shareholders are entitled to examine the stockholders' list only during the fifteen-day period immediately prior to the meeting (186a, 21a-23a), and even this privilege is meaningless as to companies like Pantepec whose shares are in bearer form (31a).

The Venezuelan Commercial Code from which the foregoing derives is based upon the Italian Commercial Code of 1882 (190a, 191a, 21a). Although the Italian Code relative to corporations was modified some years ago, the basic articles relative to corporations in the Venezuelan Code remain unchanged (190a). They hark back to a primitive economic era in which corporations typically had a dozen shareholders and it was calculated policy, which Venezuela still has not seen occasion to rectify, to deny small shareholders a remedy for corporate abuse (158a-159a).

Corporate litigation is rare in Venezuela (147a). In a legal treatise introduced by the defendants, the rights granted to minority shareholders by the Venezuelan Code are characterized as "futile" and "theoretical" (192a). The trial judge himself stated that it was established that plaintiffs have no remedy under the law of Venezuela (153a).

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[1] The limit of judicial power is to order the call of another stockholders' meeting (187a-188a, 21a-22a). Even this remedy is confined to (1) complaints of 20% or more of stockholders, or (2) complaints concerned solely with illegal action taken at a stockholders' meeting within the past fifteen days (*id.*).

The lengthy opinion in the court below (App. A, *infra*) makes no reference whatever to the overwhelming American interest in the controversy. For aught that therein appears, the locus of all parties concerned and of the transactions and subject matter in dispute could be Venezuela. Rejecting the grouping of contacts approach of *Auten* v. *Auten*, 308 N. Y. 155, 124 N. E. 2d 99 (1954), and its numerous progeny, and ignoring the progressively protective trend of state and federal decisional and statute law in related areas, the court below found Venezuelan law to be mandated under the "internal affairs" rule gleaned from one lower court decision, old dicta and the Restatement, *Conflict of Laws*, issued in the year 1934. Characterizing the pertinent policy of Venezuela as one "which, in effect, allows only majority stockholder actions" (App. A, *infra*, p. 37), the court below found no inconsistency with that of New York; and, further, that New York would regard Venezuela's conditions for suit as a matter of substance rather than of local procedure or remedy.

If certiorari be granted petitioners will also question the affirmance by the court below of the denial of their motion to strike the Venezuelan law defenses of respondents Buckley and Catawba, and to strike Pantepec's answer and the appearance on its behalf by its present attorneys, with leave for it to replead through independent counsel. This subject is the first dealt with in the opinion below (App. A, *infra*, pp. 25-8).

The rulings sought to be reviewed leave petitioners and other shareholders wholly without remedy for respondents' allegedly continuing self-dealing and wrongdoing.

Reasons for Granting the Writ

I.

We are keenly aware that this Court is disinclined to disturb the finding of a court of appeals as to state law. *Huddleston* v. *Dwyer*, 322 U. S. 232, 237 (1943); *Ragan* v. *Merchants Transfer and Warehouse Co.*, 337 U. S. 530, 534 (1948). We urge this case as an exception because (1) the Court of Appeals' finding of "a clearly enunciated state rule" (App. A, *infra*, p. 37) is demonstrably unsupportable; (2) in actuality, the issue of state law is of first impression and of far-reaching importance not only to the numerous shareholders of the corporation here involved but to many other American shareholders who are sure one day, if not already, to be similarly situated; (3) premised upon its fallacious finding of "a clearly enunciated state rule", the Court of Appeals deliberately and avowedly refused to pass upon the relative merits of the doctrines competing for adoption before it and expressly declared that "It is certainly not our function to apply the rule we think better or wiser" nor to be "formulating the legal policy and mind of the state" (App. A, *infra*, p. 37); (4) the Court of Appeals' rationale invites use of a foreign charter to plunder American investors and to evade the whole body of protective state and federal case and statute law; and (5) the particular issue of state law is far more likely to arise in diversity cases in the federal court than in New York or other state courts and if not reviewed by this Court it may be years before the rule adopted below is successfully challenged.

The keystone of the opinion below is the conclusion, under the heading "Internal Affairs Rule", that courts generally, and New York courts in particular, refer questions involving a shareholder's right and standing to remedy corpo-

rate fraud and mismanagement to the law of the state of incorporation. Among the New York decisions cited in this section of the opinion, however, only two present any issue involving fulfillment of conditions for maintaining a suit of this nature imposed by the chartering state. All the other New York decisions, most of them of considerable age, are cited presumably either for their dicta respecting the general application of domiciliary corporate law or simply as instances, without other relevancy, of corporate litigation where domiciliary law was applied.

The two cited cases which involved conditions of suit are *Hirshhorn* v. *Hirshhorn*, 280 App. Div. 791, 112 N. Y. S. 2d 841 (2d Dept. 1952), and *Newman* v. *Baldwin*, 13 Misc. 2d 897, 179 N. Y. S. 2d 19 (Sup. Ct. N. Y. Co. 1958).

Hirshhorn points away from, rather than toward, the conclusion below. A majority of the court therein found it unnecessary, because of inadequate proof of the foreign law, to decide whether a non-record stockholder's right to sue in behalf of a Canadian corporation should be determined by New York or Canadian law. One justice, concurring only in the result, however, was of the opinion that New York law applied, inasmuch as the corporation was engaged in business, and the acts took place and the adversary defendant resided, in New York.

Newman involved the maintainability of a derivative action in the absence of a prior demand on shareholders. It was stated that this issue was controlled by the law of Delaware, the state of incorporation which (like New York[3]) dispenses with any such demand. *Newman* was decided by Justice Owen McGivern, one of 148 *nisi prius* judges, while sitting in one of the 62 counties comprising the 10 judicial districts of the state. Decisions by New York Supreme

[3] See *Gottesman* v. *General Motors Corp.*, 268 F. 2d 194, 197-8 (2 Cir. 1959), and cases therein cited.

Court justices are in no way binding on one another (*In re Hawley's Will*; 6 Misc. 2d 927, 930, 163 N. Y. S. 2d 701, 705 (Surr. Ct. Kings Co. 1957)), and they have no force as precedents in the state Appellate Divisions and the Court of Appeals. In presenting the *Newman* case as its prime authority, the court below (App. A, *infra*, pp. 32-3) seems to have overlooked *King v. Order of United Commercial Travelers of America*, 333 U. S. 153, 161 (1947). If we correctly equate the *Newman* decision with the ruling by the South Carolina Court of Common Pleas before this Court in the *King* case, the Court of Appeals' heavy reliance on *Newman* is so seriously misplaced as to invalidate its entire solution of the state law problem.

It was petitioners' position in the courts below that the problem of state law here presented is one of first impression throughout the American jurisdictions. We contended primarily (1) for application of the grouping of contacts theory of *Auten v. Auten*, 308 N. Y. 155, 124 N. E. 2d 99 (1954), and, (2) in any event, for rejection of the Venezuelan law as repugnant to the public policy of the state. Petitioners also urged that under New York choice of law rules, especially as recently exemplified by *Kilberg v. Northeast Airlines, Inc.*, 9 N. Y. 2d 34, 172 N. E. 2d 526 (1961), the Venezuelan pre-conditions of suit should be treated as procedural and hence as not binding on the forum.

Respondents for the most part relied upon the aforementioned "internal affairs" cases cited in the opinion below.

In earlier proceedings in this case, District Judge Sugarman adopted the *Auten* doctrine without reference to the "internal affairs" rule (61a, reported 22 FRD 304); and this view was implicitly endorsed in a later ruling herein by Chief District Judge Ryan (65a). These opinions were confirmed, it seemed, by the Fifth Circuit's carefully rea-

soned adoption of the grouping of contacts theory in *Mansfield Hardwood Lumber Co.* v. *Jackson*, 268 F. 2d 317, 320-1 (1959), cert. den. 361 U. S. 885, rehearing den. 361 U. S. 926 (1960), a representative shareholders' action which would have been defeated by application of the substantive law of the state of incorporation. Even Judge MacMahon, who made the ultimate determination herein in the court of first instance, paid obeisance to the *Auten* doctrine in his opinion of June 27, 1960, although inexplicably writing that "Venezuela is the place having the most significant contacts with the subject matter and transactions in dispute" (13a).[6]

It is our basic submission on this petition that, in the posture of state law indicated above, the court below gravely misapplied the doctrine of *Erie R. Co.* v. *Tompkins* (1) by professing to discover "a clearly enunciated state rule" where in fact there is none, and (2) by deliberately refusing on that premise to fulfill its role as the counterpart of the state court of last resort.[7] Its failure to function like a state court of last resort appears in the following passage of its opinion rejecting the grouping of contacts principle (App. A, *infra*, pp. 36-7):

> "Appellants have brought to our attention a number of cases in which this Court, in order to resolve 'com-

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[6] This was the third and final District Court opinion on choice of law. The only Venezuelan contacts then and now presented by petitioners' third count (74a-80a), which was their sole concern in the court below (footnote 3, *supra*), are Pantepec's place of incorporation; the location of Pantepec's shareholders' meetings; and the location of oil concessions once owned by Pantepec, to the limited extent that their sale was the supposed basis for the fees, etc. which are the subject of one particular claim (77a-78a [par. 43]). The facts thus far adduced which reflect the overwhelming American interest are summarized on pp. 5-6, *supra*.

[7] It may be worth noting that, of the bench below, only Judge Kaufman has extensive training and experience in New York law. Judge Waterman is a Vermont lawyer; and Judge Marshall, recently designated, has been active in an entirely unrelated field.

mercial' controversies, referred to the Auten rule. But all of these cases involved questions concerning the law governing contracts or liability for torts. None of them directly or indirectly suggests that this Court was of the opinion that New York tribunals have introduced the Auten rule into corporate stockholder litigation. And appellants have not cited any decisions by New York courts in which this has been done. We do not wish to be understood as intimating in any way that the Auten rule could or could not be applied profitably to some corporate questions. Nor do we pass judgment upon the relative merits of the 'internal affairs' doctrine, vis-a-vis the Auten rule except to note our disagreement with appellants' suggestion that the 'internal affairs' doctrine has no application to the branch of the law with which we are dealing, or that it clearly serves no useful purpose at all. We think it is generally agreed that, in fact, 'the values of predictability and ease of application are best served by this rule.' Reese and Kaufman, supra, at p. 1144 [of 58 Columb. L. Rev.].[8]

In any event, the proper function of this Court is to ascertain what New York law is, and not to speculate about what it will be, or in Learned Hand's felicitous phrase, 'to embrace the exhilarating opportunity of anticipating a doctrine which may be in the womb of time, but whose birth is distant.' Spector Motor Service v. Walsh, 139 F. 2d 809, 823 (2nd Cir. 1943)

[8] The article referred to expressly confines itself to corporations doing business in two or more states in this country (pp. 1118, 1126, 1143). It urges application by a second state of the law of the state of incorporation on a highly selective basis—mainly in controversies where uniform treatment of shareholders is obviously desirable. Examples are questions as to legality of dividends, validity of proxies and extent of shareholders' liability. Minority shareholders' suits are in no way mentioned.

(dissent), vacated 323 U. S. 101 (1944). It is certainly not our function to apply the rule we think better or wiser. Klaxon Co. v. Stentor Electric Mfg. Co., supra, at p. 497. If we were to apply the Auten rule as appellants ask, we would be formulating the legal policy and mind of the state in an area where there would appear to be a clearly enunciated state rule. Yoder v. Nu-Enamel Corp., 117 F. 2d 488, 489 (8th Cir. 1941)." [footnotes omitted]

The "clearly enunciated state rule" adverted to at the conclusion of the quotation is the supposed principle of mechanical referral to the law of the state of incorporation. In view of what precedes that reference, the Court of Appeals, in denying petitioners any day in court, must have deemed inapplicable this Court's admonitions to seek the developing line of authority from all available data. *West* v. *American Telephone and Telegraph Co.*, 311 U. S. 223, 237 (1940); *Bernhardt* v. *Polygraphic Co.*, 350 U. S. 198, 204-5 (1955); *Meredith* v. *Winter Haven*, 320 U. S. 228, 237-8 (1943); see also Corbin, *The Laws of the Several States*, 50 Yale L. J. 762, 775-6 (1941). Seemingly ignored were these plain portents of New York's preference for the modern grouping of contacts concept over the much-criticized[9] "internal affairs" rubric, especially in this instance where that formula works such a spectacular failure of justice, to absolutely no juridical, constitutional, political or other end or purpose:

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[9] *Koster* v. *Lumbermen's Mutual Casualty Co.*, 330 U.S. 518, 521-2, 526-7 (1946); *Williams* v. *Green Bay & Western R. Co.*, 326 U.S. 549, 553 (1946); *Levy* v. *Pacific-Eastern Corp.*, 153 Misc. 488, 491, 275 N.Y.S. 291, 296-7 (Sup. Ct. N.Y. Co. 1934); *State ex rel. Weede* v. *Iowa Southern Utilities Co.*, 231 Iowa 784, 816-827, 2 N.W. 2d 372, 390-395 (1942); Latty, *Pseudo-Foreign Corporations*, 65 Yale L.J. 137, 144 (1955); 2 Hornstein, *Corporation Law and Practice* (1959), pp. 83-4; Notes, 33 Columb. L. Rev. 492 (1933); 44 Harvard L. Rev. 437, 439 (1931).

1. Leading New York conflict of laws decisions have shown scant regard for the 1934 *Restatement* so heavily relied on in the opinion below. *Auten* v. *Auten*, 308 N. Y. 155, 159-61, 124 N. E. 2d 99, 101-2 (1954), the landmark case, was a flat rejection of the rigid, traditional text of *Restatement, Conflict of Laws*, §332. In *Kilberg* v. *Northeast Airlines, Inc.*, 9 N. Y. 2d 34, 49, 172 N. E. 2d 526, 534 (1961), New York rejected another basic *Restatement, Conflict of Laws*, teaching, this time in the field of tort.[10] Actually, far from slavishly following the *Restatement* and older authorities, New York is the innovator and the leader in this branch of law. Tentative Draft No. 6 of *Restatement Second, Conflict of Laws* (1960), the chapter on Contracts, generally adopts New York's now widely accepted approach, in terms of the law of "the state of most significant relationship."

2. In 1961 the New York Legislature enacted the Business Corporation Law, to take effect April 1, 1963, as a recodification and modernization of existing state corporation statutes. The many innovations include, in §1317, the concept of a "domiciled foreign corporation". Such a corporation is defined as one authorized to conduct or actually conducting business in the state with at least two-thirds of its outstanding stock or two-thirds of its voting stock owned by residents of the state, or else with two-thirds of its business or investment income allocable to the state for franchise tax purposes. Such a "domiciled foreign corporation"

[10] In *Huber Baking Co.* v. *Stroehmann Bros. Co.*, 252 F. 2d 945, 951 (2 Cir. 1958), cert. den. 358 U.S. 829, the Second Circuit applied *Auten* as New York doctrine in a trademark infringement and unfair competition suit. In the opinion below (App. A, *infra*, p. 36), the court acknowledges that it has followed *Auten* in tort as well as contract cases.

is subject, under §§1318-20 of the Act, to a number of regulatory provisions applicable to domestic corporations. Under §1318 the directors and officers of such a foreign corporation will be subject to the same liability for misconduct in office as the directors and officers of a domestic corporation; *and such liability will be enforceable and relief will be granted by the New York courts in the same manner as in the case of domestic corporations.* New York is the first of the states to adopt a statutory grouping of corporate contacts for such purposes. In *Hutchison* v. *Ross*, 262 N. Y. 381, 394-5, 187 N. E. 65, 70-1 (1933), the State Court of Appeals found public policy, as expressed in a statute, to outweigh dicta in old cases. The new Business Corporation Law, although prominently urged in petitioners' briefs in the court below, is ignored in its opinion.

3. Nearly sixty years ago, New York refused to apply the "internal affairs" rule where

> "It would necessarily follow . . . that the directors of a foreign corporation transacting business and having its principal office in this state may plunder the corporation with impunity and the courts of this state are without power to redress such wrongs as appear upon the face of the complaint in this case." *Miller* v. *Quincy*, 179 N. Y. 294, 299-300, 72 N. E. 116, 118 (1904).

New York has since consistently held that claims against directors, officers and third parties for mismanagement and fraud do not involve "internal affairs". *Goldstein* v. *Lightner*, 266 App. Div. 357, 42 N. Y. S. 2d 338 (1st Dept. 1943), aff'd 292 N. Y. 670, 56 N. E. 2d 98 (1944); *Weinstein* v. *Aeolian Co.*, 243 App. Div. 355, 277 N. Y. S. 230 (2d Dept. 1935); *Frank*

v. *American Commercial Alcohol Corp.*, 152 Misc. 123, 125-30, 273 N. Y. S. 622, 624-9 (Sup. Ct. N. Y. Co. 1934); *Knobel* v. *Haïti Commerce Co., S. A.*, 89 N. Y. S. 2d 612 (Sup. Ct. N. Y. Co. 1949); *Sher* v. *Tilles*, 8 Misc. 2d 253, 166 N. Y. S. 2d 794 (Sup. Ct. Nassau Co. 1957); *Tarlow* v. *Archbell*, 47 N. Y. S. 2d 3, 7-8 (Sup. Ct. N. Y. Co. 1943), aff'd 296 N. Y. 757, 70 N. E. 2d 556 (1946); *North* v. *Ringling*, 187 Misc. 621, 624-5, 63 N. Y. S. 2d 135, 138-9 (Sup. Ct. N. Y. Co. 1946); *Ackert* v. *Ausman*, 29 Misc. 2d 974, 976-7, 218 N. Y. S. 2d 814, 817-8 (Sup. Ct. N. Y. Co. 1961).

4. Assuming *arguendo* that mechanical referral to domiciliary corporate law has some viability in New York case law, it by no means should be assumed that any such doctrine would be applied in the circumstances of this case. New York is no respecter of precedent where justice demands that a question be re-examined. *Woods* v. *Lancet*, 303 N. Y. 349, 354-5, 102 N. E. 2d 691, 694 (1951) [allowing for the first time a cause of action for pre-natal injuries]. The New York Court of Appeals has announced that a rule should be discarded when found to be "out of tune with the life about us, at variance with modern-day needs and with concepts of justice and fair dealing." *Bing* v. *Thunig*, 2 N. Y. 2d 656, 667, 143 N. E. 2d 3, 9 (1957) [abandoning the doctrine of immunity for negligence of hospital employees]. This contrasts, for example, with Massachusetts where "Principles are announced and adhered to in broad magisterial terms [with] emphasis . . . on precedent and adherence to the older ways." Wyzanski, J. in *Pomeryntz* v. *Clark*, 101 F. Supp. 341, 346 (D. Mass. 1951).

As stated in its opinion (App. X, *infra*, pp. 36-7), the court below never tried to estimate the view of the state

court of last resort in terms of the relative merits of the principle of mechanical referral to the law of the state of incorporation vis-à-vis the *Auten* rule, or to apply the rule thought to be better or wiser, or to formulate the legal policy and mind of the state. If this is sound doctrine in these circumstances, *Erie R. Co.* v. *Tompkins* has truly begotten a monstrous offspring and the worst forebodings of the early critics of that decision[11] will, at this late date, have been substantiated.

Much the same has to be said for the lower court's further finding that the Venezuelan law is compatible with New York's public policy. In *Kilberg* v. *Northeast Airlines, Inc.*, *supra*, 9 N. Y. 2d 34, 172 N. E. 2d 526 (1961), the Court of Appeals, *sua sponte*, abandoned the universal rule that the *lex loci delicti* controls the measure of damage, in order to avoid subjecting New York residents to Massachusetts' $15,000 limitation on recovery in wrongful death actions. The policy here involved cuts just as deep. See *Pomerantz* v. *Clark*, *supra*, 101 F. Supp. 341, 346-7 (D. Mass. 1951). We think it apparent that the court that decided *Kilberg* would be appalled by the denial of justice inherent in the decision below.

II

In *Kilberg* v. *Northeast Airlines, Inc.*, *supra*, 9 N. Y. 2d 34, 51, 172 N. E. 2d 526, 535 (1961), a minority of the court expressed grave doubt as to the constitutionality of the majority view in light of the apparent denial of full faith and credit to the Massachusetts damage limitation, citing *Hughes* v. *Fetter*, 341 U. S. 609 (1951).

The present case presents no such constitutional constraint or problem. Nor is application of the Venezuelan

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[11] E.g., Clark, *State Law in the Federal Courts: The Brooding Omnipresence of Erie* v. *Tompkins*, 55 Yale L. J. 267, 294-2 (1946).

code suggested, in view of the overwhelming local interest, even by the nebulous doctrine of the comity of nations (*Hilton* v. *Guyot*, 159 U. S. 113, 163-4 (1895)).

The rule announced below undermines, to absolutely no purpose, the whole body of laboriously evolved case and statutory law for the protection of small shareholders, whenever the corporation happens to be chartered in a foreign land with less concern for minority interests. The danger is a real and growing one. Hardly a day passes without the financial journals heralding the arrival of a new foreign issue in the American securities market. The small investor, always ripe for exploitation, is stripped of all protection under the decision below where the chartering nation is one of the many which have yet to cope with the grave abuses which inevitably accompany wide cleavage between the ownership and the control of corporate enterprises.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Dated, New York, N. Y.
March 20, 1962

Respectfully submitted,

FREDERICK H. BLOCK
ROBERT B. BLOCK
IRVING SONNENSCHEIN
Attorneys for Petitioners

APPENDIX A

Court of Appeals Opinion

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 174—September Term, 1961.

(Argued January 3, 1962 Decided February 13, 1962.)

Docket No. 27144

NATHAN HAUSMAN, in His Own Behalf as a Stockholder of Defendant Pantepec Oil Company, C. A., and in Behalf of All Other Such Stockholders Similarly Situated,

Plaintiff-Appellant,

—and—

JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u/w of Daniel Buckley, deceased, PETER FUNDARO, HAROLD MALTZ, NORVIN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT,

Intervenor-Plaintiffs-Appellants,

—against—

JOHN W. BUCKLEY, THE CATAWBA CORPORATION and PANTEPEC OIL COMPANY, C. A.,

Defendants-Appellees,

—and—

JOHN S. BAILEY, EDUARDO LOPEZ DE CEBALLOS, GEORGE S. MONTGOMERY, JR., JOSE MELICH ORSINI, SANTIAGO SEGOVIA, JOHN T. SINCLAIR, JR., GUY K. STEWART, R. RAMIREZ U., CECILIO VELASCO, G. J. VAN WAGENINGEN, PHILLIPS PETROLEUM COMPANY,

Defendants.

Before:

WATERMAN, KAUFMAN and MARSHALL,

Circuit Judges.

Appeal from a judgment insofar as it dismisses two counts of a complaint in a stockholders' derivative action with prejudice on the grounds that under Venezuelan law, applicable under New York conflict of laws principles, a stockholder may not bring suit on behalf of his corporation, and from the denial of certain motions, United States District Court, Southern District of New York, Lloyd F. MacMahon, *Judge*. Affirmed.

ROBERT B. BLOCK, New York, N. Y., *of counsel* (Heffner, Block & Block, Sonnenschein & Sherman, Murray W. Greif, New York, N. Y.), *for appellants*.

THOMAS W. HILL, JR., New York, N. Y. (Spear and Hill, New York, N. Y.), *for appellees John W. Buckley and The Catawba Corporation*.

JOSEPH A. MCMAHON, New York, N. Y. (Condert Brothers, New York, N. Y.), *for appellee Pantepec Oil Company, C. A.*

KAUFMAN, *Circuit Judge*:

This is a stockholders' derivative action brought on behalf of the Pantepec Oil Company, C. A. (Pantepec), a corporation organized under the laws of Venezuela. Jurisdiction is based on diversity of citizenship, 28 U. S. C. § 1332.

In the stage of this protracted litigation[1] which concerns us on this appeal, the third amended complaint contained three counts:

(1) Count 1 alleged that a certain contract between Pantepec and defendant Phillips Petroleum Company (Phillips) constituted an unlawful sale of Pantepec's assets under Venezuelan law. It demanded rescission and damages;

(2) Count 2 charged the individual defendants, officers and directors of Pantepec, with responsibility for the Phillips contract, and sought damages for a breach of fiduciary duty to the corporation;

(3) Count 3 alleged that individual defendant Buckley, and a company dominated by him, The Catawba Corporation (Catawba), caused Pantepec to enter into an unlawful management services contract with Catawba; it demanded cancellation of that agreement, and damages for corporate waste.

On November 24, 1959, Judge MacMahon denied a motion made by the plaintiffs pursuant to Rule 12(f), Fed. R. Civ. P., to strike from the answers of Pantepec, Buckley, and Catawba, defenses alleging lack of jurisdiction over Pantepec's person. Subsequently, the defendants moved for a separate and prior trial of another defense which

[1] The action was commenced on April 18, 1957. Since then a number of orders on various matters have been entered. Three of these are reported: *Dalen* v. *Bailey*, 153 F. Supp. 548 (S. D. N. Y. 1957); *Dalen* v. *Bailey*, 158 F. Supp. 204 (S. D. N. Y. 1957); *Hausman* v. *Bailey*, 22 F. R. D. 304 (S. D. N. Y. 1957).

[2] The only individual defendant before the court was John W. Buckley.

[3] The case was ultimately assigned to Judge MacMahon for all purposes, Rule 2, General Rules, S. D. N. Y.

[4] See Rule 42(b), Fed. R. Civ. P.

challenged the right of the plaintiffs, under Venezuelan law, to maintain an action on behalf of Pantepec. This motion was granted. Judge MacMahon agreed with the defendants' assertion that Venezuelan law, applicable under controlling New York conflict of laws principles, would determine the right of the plaintiffs to enforce a corporate claim; and that the content of this foreign law raised a question of "fact" which should be resolved before further proceedings on the merits of the issues raised by the complaint.

However, on April 17, 1961, the day set for the separate trial on the question of Venezuelan law, the plaintiffs moved, pursuant to Rules 12(f) and (h), Fed. R. Civ. P., to strike the defenses of Buckley, Catawba, and Phillips which contested their right to bring the action; and for the same purpose, moved to strike Pantepec's answer and an appearance entered on its behalf by certain attorneys. These motions were promptly denied, and the preliminary trial was held before Judge MacMahon, sitting without a jury.

On June 8, 1961, Judge MacMahon filed his findings of fact and conclusions of law. He held: (a) that Venezuelan law governed the merits of plaintiffs' claims; (b) that under Venezuelan law the complaint failed to state a claim entitling plaintiffs to relief on the first count (against Phillips); and (c) that under this law plaintiffs had no right to maintain an action in behalf of Pantepec on the remaining counts. Judgment for defendants was entered accordingly on June 29, 1961.

Evidence of Venezuelan law was proffered by the defendants. Plaintiffs conceded that under Venezuelan law stockholders have no right to enforce any claim in favor of their corporation against officers, directors, or third parties. Tr. p. 5[illegible]. This right is conferred exclusively upon the stockholders' meeting, which may bring suit through the appointment of persons to represent it for that purpose. Moreover, there are restrictions on the right of minority

Plaintiffs appeal from so much of this judgment dismissing counts 2 and 3 of their complaint on the grounds that they had no right to maintain an action on behalf of Pantepec, and also ask review of interlocutory orders entered November 24, 1959 and April 17, 1961, denying their motions to strike certain defenses in Pantepec's answer and the appearance of certain attorneys on its behalf.

We hold that no error was committed by the trial court below, and that the judgment for defendants must be affirmed.

A.

Appellants' first contention is that their various motions were improperly denied. However, insofar as the denial of the motion made on November 24, 1959 is concerned, it is unnecessary to determine if there was any error. Although the motion was unsuccessful in its attempt to strike defenses which contested the court's jurisdiction over the person of Pantepec, Judge MacMahon subsequently held that the court had jurisdiction over all the parties. Thus, the question raised by his denial of the motion is rendered moot.

On the other hand, the trial court's denial of appellants' motions to strike (a) Pantepec's answer, (b) the appearance on its behalf of certain attorneys, and (c) defenses raised by Buckley, Catawba, and Phillips, requires discussion. By these motions appellants sought to prevent

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stockholders to have their complaint considered by the stockholders' meeting. Although a stockholder is entitled, as of right, to have his complaint brought to the attention of the meeting, he has no right, as such, to have a statement of the facts supporting his complaint put before the meeting unless he holds one-tenth of the capital stock, or represents stockholders who do (Findings of Fact 17-32).

the defendants from contesting their right to bring the instant action on behalf of Pantepec.

The first two motions, (a) and (b), are based on the allegation that Pantepec was deprived of the benefit of independent counsel because its attorneys, until September 29, 1960, also represented the adversary defendant Buckley. Appellants contend that as a consequence, the answer to the third amended complaint (filed on September 18, 1959) which raises the defense challenging their right to bring this action, does not necessarily represent the position which Pantepec might have taken on this issue if it had availed itself of other legal counsel. In support of their argument that Pantepec may have suffered from the "conflicting" interests of counsel, appellants bring to our attention Opinion No. 842, Committee on Professional Ethics, of the Association of the Bar of the City of New York (January 4, 1960). In that Opinion, a majority of the Committee decided that an attorney's representation of both the corporation and adversary defendants in stockholders' derivative actions may be unethical. Putting aside the question as to whether such a ruling by a Committee of a Bar Association would warrant striking an answer and defenses for a violation of ethical standards, we believe that the trial court did not commit error in denying the motion to strike Pantepec's answer and the appearance of its attorneys. Appellants' reliance on Opinion 842, *supra*, is misplaced. That Opinion, as we read it, did not proscribe dual representation in all cases, but stated that the propriety of such conduct "must be determined in the light of the particular facts attending each such case."

Here the corporation was represented by the same attorneys who represented its directors during part of the preliminary stages of the litigation. It was during this period that Pantepec raised the defense which challenged

the right of stockholders to sue on its behalf. Was this defense necessarily in the best interest only of the directors, as appellants seem to suggest? We think not. Assuming that the allegations of the complaint may have had some merit, the corporation nevertheless, had a legitimate interest in protecting the right of the stockholders' meeting to bring an action on its behalf, if it were to be brought at all. As we will discuss at greater length in connection with other issues raised by the appeal,* under Venezuelan law, enforcement of a corporation's claims depends not merely upon their merit but upon a decision of the stockholders' meeting that they *ought* to be enforced.

This legitimate interest in bringing the action to a halt before the merits of the allegations are considered exists even though we may assume that an adversary defendant, represented by the same counsel, would have a different interest in seeing the litigation ended. Therefore, it is not necessarily true that Pantepec was deprived of the advice of disinterested counsel, and that it would have conducted itself differently if it were represented by another attorney. Under these circumstances, viewing the matter after a judgment has been rendered as we must, we are unable to conclude that denial of the motion to strike the defense was error. Cf. *Otis & Co. v. Penn. R.R. Co.*, 57 F. Supp. 680 (E. D. Pa. 1944) (Knoledner, *J.*); *Kelley v. 74 & 76 West Tremont Avenue Corp.*, 24 Misc. 2d 370, 198 N. Y. S. 2d 721 (Sup. Ct. 1960); *Garlen v. Green Mansions, Inc.*, 9 App. Div. 2d 760, 193 N. Y. S. 2d 116 (1st Dept. 1959).

We note, however, that this decision is limited to the facts before us, and should not be construed as voicing disagreement with Opinion 842.

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*See pp. 28-29, 38-39 *infra*.

Inasmuch as we conclude that the denial of the motion directed to Pantepec's answer was correct, it would serve no purpose to consider whether the other defendants were also entitled to raise the same defense; and we shall proceed to examine the principal issue raised by this appeal, the applicability of Venezuelan law.

B.

Since this is a diversity action, we must apply the conflict of laws principles of New York (the forum state) in order to determine whether Judge MacMahon's reference to Venezuelan law was correct. *Klaxon Co.* v. *Stentor Electric Mfg. Co.*, 313 U. S. 487 (1941); *Erie R. Co.* v. *Tompkins*, 304 U. S. 64 (1938); *Rand* v. *Underwriters at Lloyd's*, 295 F. 2d 342, 345 (2nd Cir. 1961); *Hertz* v. *Graham*, 292 F. 2d 443, 448 (2nd Cir. 1961); *Royce Chemical Co.* v. *Sharples Corp.*, 285 F. 2d 183, 186 (2nd Cir. 1960); *Ricciuti* v. *Voltare Tubes, Inc.*, 277 F. 2d 809, 810 (2nd Cir. 1960).

The specific issue with which we are concerned, pertains to the right of a stockholder of a foreign corporation to participate in its management, i.e., to bring a lawsuit on the corporation's behalf. The trial court was of the opinion that the courts of New York would characterize this as a "substantive" issue which related to the administration of the internal affairs of a foreign corporation, and that these courts would not view it as a mere question of "procedure." Consequently, Judge MacMahon held that New York conflict of laws principles, embracing the so-called "internal affairs" choice-of-law doctrine, would require him to refer to the law of Pantepec's place of incorporation (domicile), which is Venezuela.

At the outset, appellants contend that the trial court erred in its assumption that the New York courts would

have considered this issue "substantive" rather than "procedural." As they view the matter, "the substance is the corporation claim, by whoever [sic] and however asserted. The 'who' and the 'how' are merely mechanics, procedure or remedy" (Appellants' Brief p. 26). In New York procedural questions are always governed by the law of the forum. *Kilberg* v. *Northeast Airlines*, 9 N. Y. 2d 34, 172 N. E. 2d 526 (1961). Therefore, appellants conclude it was unnecessary and incorrect to apply choice-of-law rules. We disagree.

It is essential to remember that, above all, we are dealing with a question of conflict of laws policy.

> "The words 'substantive' and 'procedural' or 'remedial' are not talismanic. Merely calling a legal question by one or the other does not resolve it otherwise than as a purely authoritarian performance." *Guaranty Trust Co.* v. *York*, 326 U. S. 99, 115 (1945) (dissent).

Our real inquiry must be directed to the question whether appellants' right to bring this action involves no more than compliance with procedural requirements extraneous to the substance of their claim, or whether it concerns the very nature and quality of their substantive rights, powers and privileges as stockholders of a Venezuelan corporation. Thus defined, we think it is clear that appellants' position cannot prevail. A rule which provides that the enforcement of corporation claims through derivative actions must be undertaken pursuant to the will of a majority of its stockholders reflects a deliberate policy that such actions ought to be brought not only when the claims may have merit but when the stockholders, as a body, are of the opinion that the corporate welfare is best promoted by suing upon them.[7] The issue is not just "who"

[7] See analysis of the Massachusetts Rule by Wyzanski, *J.*, p. 39 *infra*.

may maintain an action or "how" it will be brought, but "if" it will be brought.

We think the situation analogous to the problems raised by statutes of limitation. Ordinarily, for conflict of laws purposes, the statute of limitation of the forum controls. RESTATEMENT, CONFLICT OF LAWS, §§603, 604 (1934).

> "But a statute of the place where the right arose may impose upon it a condition which goes to its substance, and, when this is so, the condition will be observed elsewhere. This has ordinarily come up in the case of statutory rights in which the limitation was imposed by the same statute which created the right itself * * * But it is not necessary that the limitation should be in the same statute, so the purpose be plain to make it a condition." *Wood & Selick, Inc.* v. *Compagnie Generale Transatlantique*, 43 F. 2d 941, 942-43 (C. C. A. 2, 1930) (L. Hand, *J.*).

See *Bournias* v. *Atlantic Maritime Co.*, 220 F. 2d 152 (2nd Cir. 1955); RESTATEMENT, *supra*, §605. In the present case we hold that the condition imposed by Venezuelan law on the right to enforce corporate claims goes to the substance of that right, and cannot be treated as dealing with the mere procedure by which the claims are enforced. Compare *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U. S. 541, 556 (1949) in which, for *Erie* doctrine purposes, it was held that a statute requiring security for expenses of stockholder litigation "so conditions the stockholder's action" that it cannot be disregarded as "a mere procedural device."

This approach to the problem is consistent with the law of New York, which recognizes that "remedial and substantial 'shade into each other constantly' and 'the law of the forum normally determines for itself' whether a given question is one of substance or procedure." *Kilberg*

v. *Northeast Airlines*, *supra*, at p. 137. In *Coster* v. *Coster*, 289 N. Y. 438, 46 N. E. 2d 509 (1943) the Court of Appeals held that a wife's right to sue her husband for personal injuries sustained in Massachusetts (and before her marriage) was a part of her substantive claim, and not a mere matter of remedy. Therefore, Massachusetts law, denying her the right to sue, was applied. Cf. *Newman* v. *Baldwin*, 13 Misc. 2d 897, 179 N. Y. S. 2d 19 (Sup. Ct. 1958) (necessity of demand on stockholders preliminary to bringing derivative action treated as substantive and choice-of-law rules applied); *Miley* v. *Adams*, 16 F. R. D. 105 (S. D. N. Y.), remanded, 217 F. 2d 647 (2nd Cir. 1954); *Bankers Nat. Corp.* v. *Barr*, 7 F. R. D. 305 (S. D. N. Y. 1945).

Cases cited by appellants suggesting that insofar as the defendants in a stockholders' derivative action are concerned, the question of "who" brings the action is merely collateral to the substance of the claims being prosecuted, are not relevant to the conflict of laws problems.[*] As Justice Frankfurter has said, the terms "substance" and "procedure" are

> "the same keywords to very different problems. Neither 'substance' nor 'procedure' represents the same invariants. Each implies different variables depending upon the particular problem for which it is used." *Guaranty Trust Co.* v. *York*, *supra*, at p. 108.

Since the trial court correctly regarded the issue of appellants' right to bring the action as being "substantive," we must examine its determination of the applicable choice-of-law rule.

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[*] *Chaplin* v. *Selznick*, 186 Misc. 66, 58 N. Y. S. 2d 453 (Sup. Ct. 1945); *Koral* v. *Savory, Inc.*, 276 N. Y. 215, 11 N. E. 2d 883 (1937); *Ripley* v. *Int'l Rys. of Central America*, 8 App. Div. 2d 310, 188 N. Y. S. 2d 62 (1st Dept. 1959), aff'd 8 N. Y. 2d 430, 171 N. E. 2d 443 (1960).

Internal Affairs Rule

The "internal affairs" choice-of-law rule, as applied to issues peculiar to disputes involving corporations, is well established and generally followed throughout this country. See Reese and Kaufman, *The Law Governing Corporate Affairs: Choice of Law and the Impact of Full Faith and Credit*, 58 Colum. L. Rev. 1118, 1125 (1958). Insofar as it pertains to the issue under consideration, it has been summarized as follows:

> "The right of a shareholder to object to conduct occurring in the operation of the corporate enterprise is determined by the law of the state of incorporation. This includes acts that are beyond the purposes of the corporation, acts which are prohibited either by the state of incorporation or by the state where the acts are to be performed and acts which are alleged to be beyond the authority of the officers or directors * * *" RESTATEMENT, CONFLICT OF LAWS, §183, comment b (1934).

See also Ehrenzweig, *Conflict of Laws*, Part One, pp. 40-41 (1959).[9]

We agree with Judge MacMahon that the courts of New York also adhere to the "internal affairs" rule. *Newman* v. *Baldwin*, *supra*, held that the law of the state of incorporation determined whether a demand for relief must be made upon a corporation's stockholders as a body be-

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[9] RESTATEMENT, *op. cit. supra*, §194:

"*Comment:*

a. Law governing shareholder's right: The existence and extent of the right of the shareholders to control the actions of the corporate officers or agents is determined by the law of the state of incorporation (see §183)."

fore a derivative action could be brought."[10] This decision, which dealt with a problem closely analogous to the present one, relied upon the provision and comment of the Restatement noted above. In addition, it cited *Russian Reinsurance Co.* v. *Stoddard*, 240 N. Y. 149, 147 N. E. 703 (1925) in which the Court of Appeals stated:

> "If the existence of the [foreign] corporation, its capacity to sue, or the authority of its directors to represent it or to bring the action is challenged, we look to the charter and the law of its corporate domicile for the data upon which we may rest our determination of such questions * * *." 240 N. Y. 154, 147 N. E. 704.

Cf. *Long Park, Inc.* v. *Trenton-New Brunswick Theatres Co.*, 297 N. Y. 174, 182, 77 N. E. 2d 633, 636 (1948) (Fuld, *J.* dissenting); *German-American Coffee Co.* v. *Diehl* (No. 1), 216 N. Y. 57, 109 N. E. 875 (1915); *Vanderpoel* v. *Gorman*, 140 N. Y. 563, 35 N. E. 932 (1894); see also *Matter of American Fibre Chair Seat Corp.*, 265 N. Y. 416, 420, 193 N. E. 253, 255 (1934): "The stockholders of a corporation may be the real owners of the corporation, but their right to control the corporation is governed by the law of its creation" (Lehman, *J.*).

Moreover, the "internal affairs" rule has been applied repeatedly in order to determine the fiduciary duty of a

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[10] A federal court must "give respectful heed to the pronouncements even of inferior state tribunals of record," *Mayer* v. *Chase National Bank*, 233 F. 2d 468, 470 (2nd Cir.), cert. denied 352 U. S. 841 (1946) and must accept as authoritative the decisions of a trial court of statewide jurisdiction "in the absence of more convincing evidence of what the state law is." *Fidelity Union Trust Co.* v. *Field*, 311 U. S. 169, 178-79 (1940); *Mayer* v. *Chase National Bank*, *supra*; *Robles* v. *Folsom*, 239 F. 2d 562, 564 (2nd Cir. 1956), cert. denied 353 U. S. 960 (1957); cf. *Beggs* v. *Dougherty Overseas, Inc.*, 287 F. 2d 80, 83 (2nd Cir. 1961).

foreign corporation's directors. *Upson* v. *Otis*, 155 F. 2d 606, 610 (C. C. A. 2, 1946); *Stratton* v. *Bertles*, 238 App. Div. 87, 263 N. Y. S. 466 (1933); *Diamond* v. *Davis*, 38 N. Y. S. 2d 103 (Sup. Ct. 1942); *German-American Coffee Co.* v. *Diehl* (No. 2), 86 Misc. 547, 149 N. Y. S. 413 (Sup. Ct. 1914), aff'd *per curiam* 168 App. Div. 913, 152 N. Y. S. 1113 (1915); *Fayes, Inc.* v. *Kline*, 136 F. Supp. 871, 872 (S. D. N. Y. 1955); and reference has been made to the law of the state of incorporation in order to resolve problems concerning one's status as a stockholder, *Milcy* v. *Adams, supra; Bankers Nat. Corp.* v. *Barr, supra;* but see *Hirshhorn* v. *Hirshhorn*, 280 App. Div. 791, 112 N. Y. S. 2d 841 (2nd Dept. 1952). In addition, New York courts for many years have dismissed a variety of actions on grounds of *forum non conveniens*, in part because of the desirability of having foreign courts apply their own law to disputes involving corporations domiciled in their jurisdictions. See *Langfelder* v. *Universal Laboratories, Inc.*, 293 N. Y. 200, 56 N. E. 2d 550 (1944); *Sternfeld* v. *Toxaway Tanning Co.*, 290 N. Y. 294, 49 N. E. 2d 145 (1943); *Novich* v. *Rojtman*, 5 Misc. 2d 1029, 161 N. Y. S. 2d 817 (Sup. Ct. 1957). Compare *Koster* v. *(American) Lumbermens Mut. Cas. Co.*, 330 U. S. 518 (1947).

Even if we were to assume, as appellants suggest, that these cases do not conclusively demonstrate that New York courts would apply the "internal affairs" rule in the present case, it would still be necessary for this Court, absent state authority directly in point, to forecast what rule they would follow in this instance. *Hablas* v. *Armour & Co.*, 270 F. 2d 71, 75-76 (8th Cir. 1959); *Yost* v. *Morrow*, 262 F. 2d 826, 828 (9th Cir. 1959); *Steinberg* v. *Hardy*, 90 F. Supp. 167, 169 (D. Conn. 1950). In view of the well established law illustrated by the cited cases and the widespread use of

the "internal affairs" rule elsewhere,[11] we believe the New York courts would adopt that rule, if they have not already done so.

Rule of Auten v. *Auten*

Appellants also maintain that the cases in which the "internal affairs" rule has been applied demonstrate only what the New York law was—and not what it is, or should be. They argue that in New York, "rigid" choice-of-law rules such as this have given way to a "flexible" formula variously described in terms of "grouping of contacts" or the finding of a "center of gravity," as enunciated in *Auten* v. *Auten*, 308 N. Y. 155, 159-61, 124 N. E. 2d 99, 101-02 (1954). This Court readily agrees that the *Auten* case has substantially changed the manner in which New York courts decide which law "governs" multistate contracts. Although it is less clear, it would appear that something in the nature of the *Auten* rule may also have been applied in tort cases. See *Kilberg* v. *Northeast Airlines, supra.* But we are unable to ascertain any authority which even remotely substantiates appellants' assertion that, "The center of gravity doctrine is encroaching on and superseding traditional conflict of laws rules in all areas of litigation" (Appellants' Brief, p. 32).

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[11] See RESTATEMENT, CONFLICT OF LAWS, §§182, 183, 194 (1934); *Perlman* v. *Feldmann*, 219 F. 2d 173, 175 (2nd Cir.), cert. denied, 349 U. S. 952 (1955) (Conn.); *Mayflower Hotel Stockholders Protective Committee* v. *Mayflower Hotel Corp.*, 193 F. 2d 666, 668 (D. C. Cir. 1951) (D. C.); *Zahn* v. *Transamerica Corp.*, 162 F. 2d 36, 40 (3rd Cir. 1947) (Del.); *Maxwell* v. *Enterprise Wall Paper Mfg. Co.*, 131 F. 2d 400, 402 (3rd Cir. 1942) (Pa.); Reese and Kaufman, *supra*, at p. 1125, n. 29; 13 Fletcher, *Corporations*, §5972 (1961); 2 Beale, *Conflict of Laws*, §192.8 (1935); but see *Mansfield Hardwood Lumber Co.* v. *Johnson*, 268 F. 2d 317 (5th Cir.), cert. denied 361 U. S. 885 (1959) (La.). Insofar as this case suggests that New York might recognize an exception for "paper" corporations, it is clear from the allegations of the complaint itself that Pantepec would not come within such an exception.

Appellants have brought to our attention a number of cases in which this Court, in order to resolve "commercial" controversies,[12] referred to the *Auten* rule. But all of these cases involved questions concerning the law governing contracts or liability for torts. None of them directly or indirectly suggests that this Court was of the opinion that New York tribunals have introduced the *Auten* rule into corporate stockholder litigation. And appellants have not cited any decisions by New York courts in which this has been done.[13] We do not wish to be understood as intimating in any way that the *Auten* rule could or could not be applied profitably to some corporate questions. Nor do we pass judgment upon the relative merits of the "internal affairs" doctrine, vis-a-vis the *Auten* rule except to note our disagreement with appellants' suggestion that the "internal affairs" doctrine has no application to the branch of the law with which we are dealing, or that it clearly serves no useful purpose at all. We think it is generally agreed that, in fact, "the values of predictability and ease of application are best served by this rule." Reese and Kaufman, *supra*, at p. 1144.[14]

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[12] *Metro Industrial Painting Corp.* v. *Terminal Construction Co.*, 287 F. 2d 382, 388 (2nd Cir. 1961); *Royce Chemical Co.* v. *Sharples Corp.*, *supra*; *Purofied Down Products Corp.* v. *Travelers Fire Ins. Co.*, 278 F. 2d 439, 441-2 (2nd Cir. 1960); *Wooten* v. *Marshall*, 279 F. 2d 558, 559 (2nd Cir. 1960); *Zoog* v. *Penn Mutual Life Ins. Co.*, 276 F. 2d 861, 864 (2nd Cir. 1960); *Huber Baking Co.* v. *Strochmann Bros. Co.*, 252 F. 2d 945, 951 (2nd Cir.), cert. denied 358 U. S. 829 (1958); *International-Rotterdam, Inc.* v. *River Brand Rice Mills, Inc.*, 259 F. 2d 137, 139 (2nd Cir. 1958), cert. denied 358 U. S. 946 (1959); *Global Commerce Corp.* v. *Clark-Babbitt Industries, Inc.*, 239 F. 2d 716, 719 (2nd Cir. 1956).

[13] Appellants cite *Haag* v. *Barnes*, 9 N. Y. 2d 554, 216 N. Y. S. 2d 65 (1961) but this case also involves contract issues.

[14] "Justification for the rule today must be sought in • • • pragmatic considerations. These, it is believed, are to be found in the demands of convenience, certainty, and ease of application. It is always desirable, and sometimes essential, that matters bearing

In any event, the proper function of this Court is to ascertain what New York law is, and not to speculate about what it will be, or in Learned Hand's felicitous phrase, "to embrace the exhilarating opportunity of anticipating a doctrine which may be in the womb of time, but whose birth is distant." *Spector Motor Service* v. *Walsh*, 139 F. 2d 809, 823 (2nd Cir. 1943) (dissent), vacated 323 U. S. 101 (1944). It is certainly not our function to apply the rule we think better or wiser. *Klaxon Co.* v. *Stentor Electric Mfg. Co.*, *supra*, at p. 497. If we were to apply the *Anton* rule as appellants ask, we would be formulating the legal policy and mind of the state in an area where there would appear to be a clearly enunciated state rule. *Yoder* v. *Nu-Enamel Corp.*, 117 F. 2d 488, 489 (8th Cir. 1941).

Public Policy

Finally, appellants contend that even if New York courts adhere to the "internal affairs" rule generally, they would refuse to apply it in this particular case for reasons of "public policy." The crux of this argument is that New York courts, which allow minority stockholder actions, would not defer to the policy of Venezuela (the corporation's domicile), which, in effect, allows only majority stockholder actions. But the courts of New York, as Judge Cardozo instructs,

> "are not free to refuse to enforce a foreign right at the pleasure of the judges, to suit the individual no-

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on the relationships *inter sese* of the corporation and its directors, officers, and stockholders be governed by a single law. This law should also be easily ascertainable, since otherwise it would be difficult, if not impossible, to foresee the legal consequences of a given course of conduct. Both of these requirements are satisfied by the application of the law of the state of incorporation." Reese and Kaufman, *supra*, at pp. 1126-27.

tion of expediency or fairness. They do not close their doors, unless help would violate some fundamental principle of justice, some prevalent conception of good morals, some deep-rooted tradition of the common weal." *Loucks* v. *Standard Oil Co.*, 224 N. Y. 99, 111, 120 N. E. 198, 202 (1918).

Appellants have not brought to our attention any case in which a New York court, in the absence of statutory direction, has held that a foreign statute governing the relations of stockholders *inter sese* in a corporation chartered in its jurisdiction "outrages the public policy of New York," *Loucks* v. *Standard Oil Co., supra*, at p. 111, and therefore cannot support a defense in an action otherwise based on that foreign law. Moreover, we are not persuaded that the Venezuelan law under consideration is "immoral" or "fundamentally unjust"[15] or that it contravenes any New York policy involving the right of stockholders to participate in the management of a corporation through the intervention of the courts.

The laws of both Venezuela and New York vest primary control of corporate affairs in the directors; create a fiduciary duty running from the directors to the corporation; and permit the stockholders to recover damages (for the corporation) for breach of that duty through resort to the courts. To be sure, access to the courts for this purpose is not unconditional in Venezuela;[16] but this is also true in New York. For example, the right of a small minority stockholder to bring suit in New York is substantially affected by a law requiring security for expenses of the litigation. N. Y. General Corp. Law, §61-b. And

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[15] *Benton* v. *Safe Deposit Bank of Pottsville*, 255 N. Y. 260, 267, 174 N. E. 648, 650 (1931).

[16] See footnote 5, *supra*.

the restrictions which both jurisdictions impose upon that right imply a fundamental agreement that corporate management ought to be protected from the abuse of this legal weapon, even though this protection is gained at the expense of the stockholders' right to protect their property. See *Lapchak* v. *Baker*, 298 N. Y. 89, 94-95, 80 N. E. 2d 751, 753 (1948).

Furthermore, there is nothing to suggest that New York courts will refuse to enforce, in appropriate cases, the so-called Massachusetts Rule, which effectively bars a derivative action unless it is approved by an independent majority of stockholders.[17] Cf. *Newman* v. *Baldwin, supra*. This rule, in many respects similar to the law of Venezuela, seeks to avoid involving the corporation in unauthorized lawsuits:

> "The fundamental basis of the rule is the Massachusetts view that neither an individual member nor a court is usually best fitted to determine whether it is to the interest of a corporation publicly to enforce corporate claims even if those claims are founded on plainly unlawful conduct participated in by corporate officers or directors . . . [The stockholder] is remitted to the directors or, if they are disqualified, to the members as a body as the appropriate tribunal to decide not only if a derivative claim has merit but if the corporate welfare is best promoted by suing upon it . . . ." *Pomerantz* v. *Clark*, 101 F. Supp. 341, 344 (D. Mass.) (Wyzanski, *J.*).

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[17] *S. Solomont & Sons Trust, Inc.* v. *New England Theatres operating Corp.*, 326 Mass. 99, 93 N. E. 2d 241 (1950); *Carroll* v. *New York, N. H. & H. R.R.*, 141 F. Supp. 456 (D. Mass. 1956); *Pomerantz* v. *Clark*, text *infra*.

We recognize that there are differences between the laws of Venezuela and those of Massachusetts,[18] but we believe the laws are fundamentally alike in conception; and that the policy they represent is not inconsistent with that of New York. It is clear that New York courts "are not so provincial as to say that every solution of a problem is wrong"[19] merely because it may differ from its own; and we find there is no substantial reason to believe that Venezuelan law would be ignored on the ground that it violates a "fundamental principle of justice."[20]

This Court cannot substitute notions of "public policy" for well established New York conflict of laws principles, and we are unwilling to conclude that this would be done by New York courts. See Paulsen and Sovern, *"Public Policy" in the Conflict of Laws*, 56 Colum. L. Rev. 969

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[18] Appellants point out that in Venezuela a majority of stockholders can prevent a court action even if they are involved in the alleged wrongdoing, but that this would not be possible in Massachusetts. Regardless of the merits of this contention, appellants have made no claim and have offered no proof that a disinterested majority of stockholders of Pantepec does not exist; and in the absence thereof we shall presume that "the majority of stockholders are * * * acting, not fraudulently, but with fair discretion in obedience to law, and in good faith toward all concerned * * *" *Bartlett* v. *New York, N. H. & H. R.R.*, 221 Mass. 530, 532, 109 N. E. 452, 453 (1915).

[19] *Loucks'* v. *Standard Oil Co., supra*, at p. 111; *Coster* v. *Coster, supra.*

[20] The recent decision in *Kilberg* v. *Northeast Airlines, supra*, does not support appellants' position in any respect. There is no indication in that case, which involved a refusal to enforce a limitation of damages prescribed by the Massachusetts wrongful death statute, that the Court of Appeals has abandoned or even modified the *Loucks* rule. In refusing to recognize a defense based upon Massachusetts law, the Court of Appeals was concerned with a strong public policy against limitation of damages for personal injuries—a policy embodied in the state constitution. Furthermore, that court appears to have preferred to rest its decision not on grounds of public policy, but on a conclusion that the damages issue was merely a matter of procedure which was controlled by the law of the forum.

(1956). In this connection we recall the wise admonition of the English judge who said, more than a century ago,

> "I, for one, protest, * * * against arguing too strongly upon public policy;—it is a very unruly horse, and when once you get astride it you never know where it will carry you. It may lead you from the sound law. It is never argued at all but when other points fail * * *" (Burrough, *J.*). *Richardson* v. *Mellish*, 2 Bing. 229, 252, 130 Eng. Rep. 294, 303 (1824).

Affirmed.

APPENDIX B

Judgment

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the thirteenth day of February one thousand nine hundred and sixty-two.

Present:

HON. STERRY R. WATERMAN,
HON. IRVING R. KAUFMAN,
HON. THURGOOD MARSHALL,

Circuit Judges.

NATHAN HAUSMAN, in His Own Behalf as a Stockholder of Defendant Pantepec Oil Company, C.A., and in Behalf of All Other Such Stockholders Similarly Situated,

Plaintiff-Appellant,

JOSEPH APPLEBAUM, *et al.*,

Intervenor-Plaintiffs-Appellants,

—v.—

JOHN S. BAILEY, *et al.*,

Defendants,

JOHN W. BUCKLEY, *et al.*,

Defendants-Appellees.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed; with costs to the appellees.

A. Daniel Fusaro
Clerk

Office-Supreme Court, U.S.
FILED
MAY 4 1962
JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

October Term, 1961

No. 805

NATHAN HALSMAN, JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u w of Daniel Buckley, deceased, PETER FUSARO, HAROLD MALTZ, NORMAN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT, in their own behalf as stockholders of Pantepec Oil Company, C. A., and in behalf of all other such stockholders similarly situated,

Petitioners

against

JOHN W. BUCKLEY, THE CATAWBA CORPORATION and PANTEPEC OIL COMPANY, C. A.,

Respondents

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR RESPONDENTS JOHN W. BUCKLEY AND THE CATAWBA CORPORATION IN OPPOSITION

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IN THE

Supreme Court of the United States

October Term, 1961

No. 805

NATHAN HAUSMAN, JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u w of Daniel Buckley, deceased, PETER FUNDARO, HAROLD MALTZ, NORVIN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT, in their own behalf as stockholders of Pantepec Oil Company, C. A., and in behalf of all other such stockholders similarly situated,

Petitioners,

against

JOHN W. BUCKLEY, THE CATAWBA CORPORATION and PANTEPEC OIL COMPANY, C. A.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR RESPONDENTS JOHN W. BUCKLEY AND THE CATAWBA CORPORATION IN OPPOSITION

Opinion Below

The opinion of the Court of Appeals for the Second Circuit is set forth in App. A of the Petition.

Jurisdiction

The jurisdictional requisites are adequately set forth in the Petition.

Question Presented

The Court of Appeals for the Second Circuit affirmed the dismissal of Petitioners' derivative action in behalf of Pantepec Oil Company C. A. ("Pantepec"), a Venezuelan Corporation, because it concluded that Venezuelan law was applicable to such an action and that under such law, it is conceded that Petitioners have no claim upon which relief can be granted. Petitioners contend, however, that Venezuelan law is not applicable. The sole question here presented, therefore, is whether, under New York conflict of laws rules, the law of Venezuela governs Petitioners' right to bring this action.

Statement

In affirming the dismissal of the third amended complaint, the Court of Appeals for the Second Circuit concluded that in a stockholders' derivative action brought in behalf of a foreign corporation, the New York Courts, if they assumed jurisdiction at all, would apply the law of the place of incorporation—in this case the law of Venezuela. The Court of Appeals then concluded that under such law Petitioners have no claim upon which relief can be granted, either in their own behalf or in behalf of Pantepec (App. to the Petition, pp. 21-41).

Petitioners contend, however, that the New York Courts would not have applied the law of Venezuela to determine whether they have a claim upon which relief can be granted. Since it is conceded by Petitioners that the complaint does not state a cause of action under the law of Venezuela, the sole question presented is the applicability of Venezuelan law under New York conflict of laws principles.

In support of their application for certiorari, Petitioners urge that:

(1) New York does not follow the rule requiring the application of the law of the place of incorporation in derivative actions;

(2) The "contacts" of the corporate defendant are with New York and this requires application of New York corporate law;

(3) The New York Business Corporation Law requires the application of New York corporate law principles; and

(4) In any event, the law of Venezuela is repugnant to the public policy of New York and would be rejected by the New York Courts.

These points are answered *seriatim* in this brief.

Argument

The issue presented in this case is a narrow one involving the interpretation of the law of the State of New York and no amount of argument can turn it into one justifying review by this Court on a writ of certiorari. The only question here presented is whether the United States Court of Appeals for the Second Circuit correctly interpreted New York conflict of laws principles in holding that New York would apply the law of Venezuela in determining whether or not Petitioners had stated a claim upon which relief could be granted. There is not the slightest doubt that the decision below correctly applied long settled principles of New York conflicts law, and there is no question of New York law requiring decision by this Court.

I

The Decision Below is Clearly Correct.

A

The law of Venezuela governs this action.

The conflict of laws rule applied by the New York courts in cases such as this is settled: In a stockholders' derivative action brought on behalf of a foreign corporation, the Court, if it assumes jurisdiction at all, will apply the law of the place of incorporation—in this case, the law of Venezuela. *Upson* v. *Otis*, 155 F. 2d 606 (2d Cir. 1946); *Russian Reinsurance Co.* v. *Stoddard*, 240 N. Y. 149, 154, 147 N. E. 704 (1925); *German-American Coffee Co.* v. *Diehl*, 216 N. Y. 57, 63-64, 109 N. E. 875 (1915); *Vanderpoel* v. *Gorman*, 140 N. Y. 563, 35 N. E. 932 (1894); *Newman* v.

Baldwin, 13 Misc. 2d 897, 179 N. Y. S. 2d 19 (Spp. Ct. N. Y. Co. 1958); Restatement, *Conflict of Laws*, § 183, Comment (b); *id.* § 194, Comment (a); *id.* § 195; *id.* § 197; *id.* § 199.

The Restatement, *Conflict of Laws*, § 183, Comment (b) (1934) provides as follows:

> "The right of a shareholder to object to conduct occurring in the operation of the corporate enterprise is determined by the law of the state of incorporation. This includes acts that are beyond the purposes of the corporation, acts which are prohibited either by the state of incorporation or by the state where the acts are to be performed and acts which are alleged to be beyond the authority of the officers or directors * * *."

In *Newman* v. *Baldwin*, *supra*, the New York Supreme Court held that the adequacy of a complaint in a stockholders' derivative action was to be tested by the law of the state of incorporation. In that case the defendant moved to dismiss the complaint on the grounds that Delaware law governed, since a Delaware corporation was involved, and that Delaware law required that a demand be made by the stockholders. The New York Court deferred decision on this question awaiting a pending Delaware appeal in a case dealing with the issue of demand. The Delaware case was decided and the New York court held, based on the Delaware determination, that no demand was required under Delaware law. The New York court flatly stated (p. 898): "This Court is of the view that Delaware law governs."

The decision in *Newman* relied in part on *Russian Reinsurance Co.* v. *Stoddard*, *supra*, in which the New York Court of Appeals had stated (p. 154):

> "If the existence of the [foreign] corporation, its capacity to sue, or the authority of its directors to represent it or to bring the action is challenged, we look to the charter and the law of its corporate domicile for the data upon which we may rest our determination of such questions * * *."

And in *Matter of American Fibre Chair Seat Corp.*, 265 N. Y. 416, 193 N. E. 253 (1934), the New York Court of Appeals wrote (p. 420):

> "The stockholders of a corporation may be the real owners of the corporation, but their right to control the corporation is governed by the law of its creation".

Upson v. *Otis*, *supra*, was a stockholder's derivative action brought in the United States District Court for the Southern District of New York by a stockholder of a Delaware corporation against some of its directors. The Court of Appeals for the Second Circuit held that the New York conflict of laws rule required the application of Delaware law, stating (p. 610):

> "Under Erie R. Co. v. Tompkins, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, 114 A. L. R. 1487, we must * * * look to New York decisions. It would seem that they follow the usual conflict of laws rule in referring to Delaware 'law' to determine the fiduciary obligations of directors of a Delaware corporation."

It is apparent from the foregoing that Petitioners' claim that the question of New York State law presented is one of "first impression" (Petition, pp. 9, 11), is without any basis. There is, instead, as the Court below held, "a clearly enunciated state rule", requiring the application of Venezuelan law (App. to Petition, p. 37).

B

The "contacts" theory of conflicts has no application here.

In their effort to avoid the unanimity of New York decisions holding that the law of the place of incorporation governs stockholders' actions on behalf of foreign corporations, Petitioners argue that the "center of gravity" or "grouping of contacts" theory applies. Petitioners are in error. The "contacts" theory is inapplicable to actions of this type.

The cases heretofore cited hold, as do all the relevant New York cases, that in a derivative action on behalf of a foreign corporation, the law of the place of incorporation applies. No New York case has applied the "contacts" theory under facts similar to those here presented.

The case cited by petitioners does not support their claim that the "contacts" theory is applicable. In *Auten* v. *Auten*, 308 N. Y. 155, 124 N. E. 2d 99 (1954), the case on which Petitioners principally rely, the New York Court of Appeals carefully limited application of the contacts theory to the facts before it, which were materially different from those involved here.

It is with good reason that the contacts theory has not been applied in New York to stockholder derivative actions. Application in derivative actions of the law of corporate domicile by all courts, regardless of where the action may be tried, has created the certainty which has permitted development of modern corporate enterprise with contacts in many jurisdictions. The rule should not be upset by application of any theory which will give an unpredictable result (see pp. 13-14 hereof).

But even if this Court should choose to apply the contacts theory as enunciated in *Auten*, it is clear on the face of the complaint that all the significant contacts in this case are with Venezuela. No trial is necessary to determine this fact and the District Court was correct in so holding (Petitioners' App. in the Court below, p. 13a).

The relevant Venezuelan contacts disclosed by the record are as follows:

1. Pantepec was created and exists under the law of Venezuela; its primary purpose was and is to engage in the business of producing and selling crude oil and natural gas in Venezuela (Petitioners' App. in the Court below, pp. 66a, 67a).

2. Before the agreement with Phillips Petroleum Company, Pantepec was engaged in the business of producing and selling crude oil and natural gas, principally in Venezuela (Petitioners' App. in the Court below, pp. 66a-78a).

3. By agreement with Phillips Petroleum Company, Pantepec sold to Phillips the oil properties of Pantepec located in Venezuela, reserving to Pantepec in Venezuela (a) an oil payment out of 10% of the production of the Venezuelan properties and (b) royalties on part of the production from new wells which may be drilled by Phillips on Venezuelan properties (Petitioners' App. in the Court below, p. 67a).

Mansfield Hardwood Lumber Co. v. *Jackson*, 268 F. 2d 317 (5th Cir. 1959), cert. denied, 361 U. S. 885 (1960), on which Petitioners rely for their conclusion that the "contacts" theory is here applicable, is plainly not in point.

There, "* * * the only contact point with the incorporating state [was] the naked fact of incorporation" (268 F. 2d at 312). Moreover, *Mansfield* was not even a stockholders' derivative action.

C

The New York Business Corporation Law is not applicable.

Petitioners rely on the New York Business Corporation Law which will become effective on April 1, 1963 to support their argument that the public policy of New York requires the application of New York corporate law to determine the right of Petitioners to maintain this action (Petition, pp. 15-16). However, the sections cited by Petitioners could not, under any circumstances, apply to Pantepec. These sections will apply only to foreign corporations which are authorized to do business, or are actually doing business, in New York. Further, they will apply only if 2/3 or more of the shares of the foreign corporation's stock are owned by residents of New York or if 2/3 or more of the corporate income is allocable to New York for franchise tax purposes. It is not alleged that any of these requirements are met in this case.

The sections cited by Petitioners, therefore, could not apply to this case even if the Business Corporation Law were presently effective.

Moreover, since New York has codified in detail, after long and exhaustive study, those circumstances under which the directors of foreign corporations will be liable under New York law, and since it is apparent that Pantepec does

not fall within the new provisions, the conclusion necessarily follows that even if the New York Business Corporation Law were now in effect, the New York Courts would apply Venezuelan law to the instant action. This is confirmed by the following excerpt from the Report of the Joint Legislative Committee to Study Revision of Corporation Laws, found at p. 31 of McKinney's Business Corporation Law:

> "A new distinction has been drawn between 'domiciled foreign corporations' and other foreign corporations (Sec. 1317). The former, at least two-thirds of whose outstanding shares, or voting shares, are owned by residents of this state or two-thirds of whose business or investment income is allocable to this state, are subjected to the same provisions as domestic corporations in regard to disclosure of financial information and liability and indemnification of officers and directors."

Thus, as to any foreign corporation which is not a "domiciled foreign corporation"—and it is clear that Pantepec is not a "domiciled foreign corporation"—it is the policy of the legislature that the well settled New York rule which requires the application of the law of the place of incorporation continues in force.

D

The law of Venezuela is not repugnant to the public policy of New York.

Petitioners argue that the New York Courts would not apply the law of Venezuela because it is repugnant to the law of the State of New York; they characterize the applicable Venezuelan law as an instrument by which large stockholders may suppress minority stockholders with impunity. In this attempt, Petitioners have allowed themselves to present something less than an accurate description of the Venezuelan law (Petitioners' App. in the Court below, pp. 15a-24a, 147a-165a; Respondents' App. in the Court below, pp. 2a-36a).

Petitioners assert that under the Venezuelan law only holders of 10% or more of the stock of a Venezuelan corporation have any right to lay a complaint before the stockholders' meeting (Petition, pp. 6-7). The fact is that each individual stockholder has the right to be heard at stockholders' meetings and, as a matter of practice, to place his complaint and the basis therefor before the stockholders in advance of the meeting (Petitioners' App. in the Court below, pp. 158a, 162a, 168a; Respondents' App. in the Court below, 15a, 17a).

If a stockholder with a complaint is able to secure the support of 10% of the stockholders, he has the right, as a matter of Venezuelan law, to have the substance of his complaint, and the facts supporting it, presented to the stockholders in advance of the meeting (Petitioners' App. in the Court below, pp. 149a-158a, 188a-199a). Petitioners assert that before this may be done, the complaining stock-

holders must deposit their stock with the comisario* in Venezuela (Petition, pp. 6-7). The fact is that such deposit is not required (Petitioners' App. in the Court below, pp. 156a-157a).

Petitioners now have, and have had during all the years since they brought this action in 1957, ample opportunity within the framework of Venezuelan law to make their grievance known to other stockholders of Pantepec. Their failure to solicit other stockholders cannot be accepted as a demonstration that Venezuelan law "deliberately throttles minority shareholders and leaves them without any practical remedy against managerial fraud" (Petition, pp. 3-4). Although a proxy solicitation might be costly, it would be no more costly than would the same procedure in an American corporation of equal size, and it is difficult to imagine a proxy solicitation which would even approach the cost of this action.

Despite differences in techniques of implementation, the fundamental or underlying policy seems to be the same under the common law of New York and the civil law of Venezuela. Neither gives stockholders the right to sue directly in their own right and each places restraints upon the ability of stockholders to interfere with corporate management: Both attempt, through differing methods, to provide a check on improvident or illegal corporate man-

* The comisario is an official appointed by the stockholders' meeting to watch over management in behalf of all the stockholders (Petitioners' App. in the Court below, p. 150a). His position is regarded with distinction (Respondents' App. in the Court below, p. 157a) and holders of the position jealously guard its integrity (Respondents' App. in the Court below, p. 158a). For failure to discharge his duties with respect to stockholders' complaints, the comisario is civilly liable to the stockholders (Respondents' App. in the Court below, pp. 18a-20a).

agement. Both attempt to protect the financial integrity of the corporate enterprise, and it is unnecessary for the purpose of deciding this case to determine which, if either, system realizes the common aims more effectively.

Furthermore, there is, as the Court below pointed out, nothing to indicate that New York would decline to enforce the law of Massachusetts, which law is similar to the law of Venezuela in that it bars minority stockholders' derivative actions unless an independent majority of stockholders has approved the institution of the action. *S. Solomont & Sons Trust, Inc.* v. *New England Theatres Operating Corp.*, 326 Mass. 99, 93 N. E. 2d 241 (1950); *Pomerantz* v. *Clark*, 101 F. Supp. 341 (D. Mass. 1951); *Carroll* v. *New York, N. Ha. & H. R. R.*, 141 F. Supp. 456 (D. Mass. 1956).

Accordingly, it is plain that Venezuelan law is not repugnant to the public policy of New York. In point of fact, the public policy arguments strongly favor the rule requiring the application of the law of the state of incorporation. Since corporate officers and directors may incur substantial personal liability for corporate decisions which, although undertaken in good faith, later prove to have been improper or illegal, it is extremely important that corporate management be able to evaluate in advance the propriety of corporate action. Any conflict of laws rule which did not afford that certainty would hamstring corporate action in an age in which nearly every large enterprise has international aspects.

Application of the law of the place of incorporation to determine the rights of stockholders, the powers of the corporation or its officers and directors, the nature and extent of the fiduciary obligations of officers and directors

and similar matters, provides a certainty of result which permits intelligent management decision and provides uniform treatment for stockholders of foreign corporations wherever they may be situated.

It is apparent, therefore, that the application of the law of Venezuela in this case is firmly grounded in reason and cannot be said to be repugnant to the public policy of New York.

In any event, in connection with Petitioners' "public policy" argument, the observation of the court below is very much in point (App. to the Petition, pp. 40-41):

> "This Court cannot substitute notions of 'public policy' for well established New York conflict of laws principles, and we are unwilling to conclude that this would be done by New York courts. See Paulsen and Sovern, '*Public Policy*' *in the Conflict of Laws*, 56 Colum. L. Rev. 969 (1956). In this connection we recall the wise admonition of the English judge who said, more than a century ago,
>
> > 'I, for one, protest, * * * against arguing too strongly upon public policy;—it is a very unruly horse, and when once you get astride it you never know where it will carry you. It may lead you from the sound law. It is never argued at all but when other points fail * * *' (Burrough, J.). *Richardson* v. *Mellish*, 2 Bing. 229, 252, 130 Eng. Rep. 294, 303 (1824)."

II.

In any Event, this Case is not a Proper one for Certiorari.

Even if it is assumed—which assumption is contrary to fact—that the law of New York on the issue of whether or not its courts would apply the law of Venezuela to this action is not entirely settled, it is nevertheless plain that this case is not one justifying review on certiorari.

This Court has stated on numerous occasions that when interpreting state law, it will rely on the construction of such law adopted by the lower federal courts because these courts are more familiar with such law. *United States* v. *Durham Lumber Co.*, 363 U. S. 522, 526-7 (1959); *Propper* v. *Clark*, 337 U. S. 472, 486-9 (1948); *Estate of Spiegel* v. *Comm'r*, 335 U. S. 701, 707-8 (1948); *Huddleston* v. *Dwyer*, 322 U. S. 232, 237 (1943).

Thus, in *Huddleston* it was said that (p. 273), "ordinarily we accept and therefore do not review, save in exceptional cases, the considered determination of questions of state law by the intermediate federal appellate courts". And in *Propper*, this Court wrote that (p. 486), "In dealing with issues of state law * * *, we are hesitant to overrule decisions by federal courts skilled in the law of particular states unless their conclusions are shown to be unreasonable."

Robertson and Kirkham, *Jurisdiction of the Supreme Court of the United States*, p. 650 (1951) declare "certiorari will not issue in diversity cases merely to review

decisions of Courts of Appeals on questions of state law, unless they appear clearly to conflict with those of the state courts."

This is hardly an "exceptional" case or one involving an "unreasonable" decision. Furthermore, even Petitioners do not argue that the decision below is in "conflict" with the decisions of the New York courts.

What then is Petitioners' argument in favor of the granting of certiorari? It is simply that the highest New York Court has not definitively spoken on the issue presented and that the courts below erred in holding that there was, under New York law, a "clearly enunciated rule" (Petition, pp. 9-14).

However, this argument, even assuming its correctness, is not a sufficient reason for issuing a writ of certiorari. Four federal judges, all—Petitioners' argument to the contrary notwithstanding (Petition, p. 12)—skilled in the law of New York, have unanimously held that the New York courts would, if faced with the facts herein presented, apply the law of Venezuela to determine Petitioners' rights. It is submitted, accordingly, that even if the law of New York was not entirely clear, this case would not be a proper one for certiorari in view of the policy of this Court to "leave undisturbed [the] Court of Appeals holding on a question of state law" (*Estate of Spiegel*, p. 708).

Conclusion

For the foregoing reasons, it is submitted that the Petition for a writ of certiorari should be denied.

Respectfully submitted,

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New York, N. Y.
April 30, 1962

Supreme Court, U.S.
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JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

October Term, 1961

No. 805

NATHAN HAUSMAN, JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u/w of Daniel Buckley, deceased, PETER FUNDARO, HAROLD MALTZ, NORVIN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT, in their own behalf as stockholders of Pantepec Oil Company, C. A., and in behalf of all other such stockholders similarly situated,

Petitioners,

against

JOHN W. BUCKLEY, THE CATAWBA CORPORATION and PANTEPEC OIL COMPANY, C. A.,

Respondents.

BRIEF OF RESPONDENT PANTEPEC OIL COMPANY, C. A. IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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IN THE

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No. 805

NATHAN HAUSMAN, JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u w of Daniel Buckley, deceased, PETER FUNDARO, HAROLD MALTZ, NORVIN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT, in their own behalf as stockholders of Pantepec Oil Company, C. A., and in behalf of all other such stockholders similarly situated,

Petitioners,

against

JOHN W. BUCKLEY, THE CATAWBA CORPORATION and PANTEPEC OIL COMPANY, C. A.,

Respondents.

BRIEF OF RESPONDENT PANTEPEC OIL COMPANY, C. A. IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Question Presented

The sole question presented is whether the court below correctly held, in affirming a judgment dismissing a minority shareholders' action brought on behalf of a Venezuelan corporation, that New York conflict of laws principles required the application of domiciliary Venezuelan law to determine the right to maintain the action in a New York federal court.

The subsidiary "Questions Presented", as stated by petitioners, are argumentative in form and were necessarily disposed of by the decision below.

Statement of the Case

The original complaint[1] in this suit was filed in the United States District Court for the Southern District of New York on April 18, 1957. The third amended complaint (66a)[2], on the basis of which the determinations below were made, was served on May 15, 1959.

The petitioners are minority stockholders of respondent Pantepec Oil Company, C. A., a Venezuelan business corporation. In their third amended complaint on behalf of Pantepec, petitioners invoked federal jurisdiction on the ground of diversity of citizenship and charged, in three counts:

1. That a certain contract between Pantepec and defendant Phillips Petroleum Company constituted an unlawful sale under Venezuelan law of Pantepec's Venezuelan properties (66a); rescission and damages were demanded (81a);

2. That the individual defendants, officers and directors of Pantepec (only one of whom, director John W. Buckley, was before the court), were responsible to Pantepec in having caused Pantepec to enter into the Phillips contract (71a); damages for breach of a fiduciary duty to the corporation were demanded (81a);

3. That defendant Buckley and a company allegedly dominated by him, The Catawba Corporation, caused Pantepec to enter into an unlawful management services contract with Catawba (74a); cancellation of that agreement and damages for corporate waste were demanded (81a).

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[1] Appendix A to respondent's brief in the court below.

[2] Numbers followed by "a" refer to the Appendix to petitioners' brief as appellants in the court below.

Plaintiffs made no application to the stockholders for relief (70a), nor did they claim that a disinterested majority of stockholders does not exist.[3]

In their answers to the third amended complaint, all of the defendants set up affirmative defenses contesting the right of the plaintiffs to maintain the action under the law of Venezuela (94a, 123a, 4a). Under Rule 2 of the General Rules of the District Court for the Southern District of New York, the case was assigned for all purposes to Judge Lloyd F. MacMahon. Thereafter, upon motion of the defendants, Judge MacMahon decided on June 27, 1960 that Venezuelan law, applicable under controlling New York conflict of laws principles, would determine the right of the plaintiffs to enforce a corporate claim; and that the content of this foreign law raised a question of fact which should be resolved at a separate trial before further proceedings on the merits of the issues raised by the complaint (12a).

However, on April 17, 1961, the day set for the separate trial on the question of Venezuelan law, plaintiffs moved to strike the defenses of Buckley, Catawba and Phillips which contested their right to bring the action; and also moved to strike Pantepec's answer and the appearance entered on its behalf by its attorneys (130a). These motions were promptly denied at the preliminary trial held before Judge MacMahon, sitting without a jury (137a, 184a).

At the trial, plaintiffs conceded that under Venezuelan law stockholders have no right to enforce any claim in favor of their corporation against officers, directors or third parties (138a). Nevertheless, defendants presented proof establishing that the right to enforce a claim in favor of a Venezuelan corporation is vested exclusively in the stockholders' meeting, which may bring suit through the appointment of persons to represent it for that purpose (19a-20a).

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[3] Appendix A to Petitioners' brief, p. 40, ftn. 18.

On June 8, 1961 Judge MacMahon filed his findings of fact and conclusions of law (15a). Although finding that, under the Venezuelan law, there are various substantive rights accorded to a stockholder of a Venezuelan business corporation to take action with respect to wrongful conduct by its officers or directors or by a stockholders' meeting, he specifically found (23a):

> "30. No single stockholder or group of stockholders of a Venezuelan business corporation is granted any right under the Venezuelan Commercial Code or any other provision of Venezuelan law which entitles him or them to maintain an action either in behalf of himself or themselves, or in behalf of the corporation, for damages allegedly caused to the corporation by its directors, officers or third parties.
>
> "31. The foregoing findings reflect the policy of the Venezuelan law to the effect that neither an individual stockholder nor the court is best fitted to determine whether it is to the interest of a Venezuelan business corporation to enforce corporate claims even if those claims are founded on plainly unlawful conduct participated in by corporate officers and directors; that only the stockholders' meeting may decide not only if the claims have merit but also if the collective corporate welfare is best promoted by suing upon them.
>
> "32. Assuming the truth of the allegations of each of the counts of the complaint herein, except for allegations as to the content and effect of Venezuelan law, a minority shareholder, upon any theory under the law of Venezuela, may not maintain an action for any of the relief prayed for in the complaint."

Judgment for defendants was entered on June 29, 1961.

Thereafter, plaintiffs appealed from so much of the judgment as dismissed counts 2 and 3 of their complaint, preferring not to appeal from the dismissal of the first count which was directed only against Phillips (8a). In

effect, therefore, plaintiffs by this means discontinued their derivative action against Phillips.

The Court of Appeals, by unanimous decision, with a carefully reasoned opinion written by a member of that court who admittedly "has extensive training and experience in New York law",[4] considered the contentions which petitioners now raise in this Court, and rejected them. On the basis of conclusive New York and federal authorities, the court agreed with the trial judge that reference should be made to Venezuelan law, since petitioners' right to bring the action concerned the very nature and quality of their substantive rights, powers and privileges as stockholders of a Venezuelan corporation; that the courts of New York adhere to the "internal affairs" choice-of-law rule; that the New York "grouping of contacts" doctrine is not applicable to corporate stockholder litigation; and that New York courts would not refuse, for reasons of public policy, to apply Venezuelan law in this particular case.

Argument

Essentially, petitioners' request for certiorari is based upon the simple assertion that, since the Court of Appeals of New York has not passed upon the identical question presented herein, the federal court below in rejecting their arguments has refused to fulfill its "role as the counterpart of the state court of last resort."[5]

Even if this assertion were not completely refuted by the wealth of authorities cited in the opinion below, no valid reasons are stated in the petition which should incline this Court to grant certiorari.

All that is involved in this case is a question of state law on which petitioners have received the considered de-

[4] Petitioners' brief, p. 12, ftn. 7.

[5] Petitioners' brief, p. 12.

termination of two federal courts. This is not a case involving a conflict among circuits in the determination of a reviewable question, and no "important question of local law in any way probably in conflict with applicable local decisions" is involved. See *Ruhlin* v. *N. Y. Life Ins. Co.*, 304 U. S. 202, 206 (1938). There is no occasion for review. *Huddleston* v. *Dwyer*, 322 U. S. 232 (1944); *Bernhardt* v. *Polygraphic Co., of America*, 350 U. S. 198 (1955).

Petitioners' criticism of the reliance of the court below on *Newman* v. *Baldwin*, 13 Misc. 2d 897, 179 N. Y. S. 2d 19 (Sup. Ct. N. Y. Co. 1958), among numerous other decisions, is ill-founded. Although petitioners sought no reargument of the decision below, they now claim[6] that the court seems to have overlooked the decision of this Court in *King* v. *Order of United Commercial Travelers of America*, 333 U. S. 153, 161 (1948). But *King* held merely that a federal court of appeals is not required to follow an unreported decision by a South Carolina county court of common pleas where there was nothing in the decisions of the South Carolina Supreme Court inconsistent with a contrary view based upon " 'reason and the very considerable authority' from other jurisdictions." *Ibid*, p. 156. *King* is entirely consistent with *West* v. *American Telephone & Telegraph Co.*, 311 U. S. 223, 236 (1940) in which this Court remarked:

> "A state is not without law save as its highest court has declared it. There are many rules of decision commonly accepted and acted upon by the bar and inferior courts which are nevertheless laws of the state although the highest court of the state has never passed upon them. In those circumstances a federal court is not free to reject the state rule merely because it has not received the sanction of the highest state court, even though it thinks the rule is unsound in principle or that another is preferable."

---

[6] Petitioners' brief, p. 11.

Indeed, the court below clearly recognized its duty in stating that "a federal court must 'give respectful heed to the pronouncements even of inferior state tribunals of record,' *Mayer* v. *Chase National Bank*, 233 F. 2d 468, 470 (2d Cir.), cert. denied 352 U. S. 841 (1956) * * *."[7]

Petitioners' contention that the court should have searched for a "developing line of authority" in New York overlooks the primary duty of a federal court "to ascertain from all the available data what the state law is and apply it rather than to prescribe a different rule, however superior it may appear from the viewpoint of 'general law' * * *." *West, supra*, p. 237. In this respect, the court below performed its duty precisely:

> "Even if we were to assume, as appellants suggest, that these cases do not conclusively demonstrate that New York courts would apply the 'internal affairs' rule in the present case, it would still be necessary for this Court, absent state authority directly in point, to forecast what rule they would follow in this instance. *Hahlas* v. *Armour & Co.*, 270 F. 2d 71, 75-76 (8th Cir. 1959); *Yost* v. *Morrow*, 262 F. 2d 826, 828 (9th Cir. 1959); *Steinberg* v. *Hardy*, 90 F. Supp. 167, 169 (D. Conn. 1950). In view of the well established law illustrated by the cited cases and the widespread use of the 'internal affairs' rule elsewhere, we believe the New York courts would adopt that rule, if they have not already done so."[8]

In the first instance, the court below held that, under New York law, the issue as to the right of a stockholder of a foreign corporation to sue on the corporation's behalf was a matter of substantive rather than procedural law. The decisions relied upon fully support this decision. *Coster* v. *Coster*, 289 N. Y. 438, 46 N. E. 2d 509 (1943). See *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U. S. 541, 556 (1949); *Wood & Selick, Inc.* v. *Compagnie Generale*.

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[7] Appendix A to Petitioners' brief, p. 33, ftn. 10.

[8] Appendix A to Petitioners' brief, pp. 34-5.

Transatlantique, 43 F. 2d 941, 942-3 (C. C. A. 2, 1930). Cf. *Newman* v. *Baldwin*, 13 Misc. 2d 897, 179 N. Y. S. 2d 19 (Sup. Ct. N. Y. Co. 1958); *Milty* v. *Adams*, 16 F. R. D. 105 (S. D. N. Y.), *remanded*, 217 F. 2d 647 (2d Cir. 1954); *Bankers Nat. Corp.* v. *Barr*, 7 F. R. D. 305 (S. D. N. Y. 1945).

Petitioners' main disagreement with the reasoning of the court below is concerned with the application of the "internal affairs" rule, instead of the "contacts" theory of *Auten* v. *Auten*, 308 N. Y. 155, 124 N. E. 2d 99 (1954), to the issue of their right to maintain a stockholders' derivative action. The careful research indicated in the opinion below, however, confirms the propriety of rejection of the *Auten* theory in favor of the clearly enunciated "internal affairs" rule under New York law. *Newman* v. *Baldwin*, *supra*, merely reflects the firmly established principle that the right of a stockholder to object to corporate conduct is determined by the law under which the corporation was created. *Russian Reinsurance Co.* v. *Stoddard*, 240 N. Y. 149, 147 N. E. 703 (1925). Cf. *Long Park, Inc.* v. *Trenton-New Brunswick Theatres Co.*, 297 N. Y. 174, 182, 77 N. E. 2d 633, 636 (1948); *German-American Coffee Co.* v. *Diehl (No. 1)*, 216 N. Y. 57, 109 N. E. 875 (1915); *Vanderpool* v. *Gorman*, 140 N. Y. 563, 35 N. E. 932 (1894); see also *Matter of American Fibre Chair Seat Corp.*, 265 N. Y. 416, 420, 193 N. E. 253, 255 (1934).

Moreover, the "internal affairs" rule has been consistently applied by New York federal courts as requiring reference to the law of the place of incorporation. See *Upson* v. *Otis*, 155 F. 2d 606 (2d Cir. 1946); *Koster* v. *(American) Lumbermens Mut. Casualty Co.*, 153 F. 2d 888 (2d Cir. 1946), *aff'd*, 330 U. S. 518 (1947); *Bankers Nat. Corp.* v. *Barr*, 7 F. R. D. 305 (S. D. N. Y. 1945); *Milty* v. *Adams*, 16 F. R. D. 105 (S. D. N. Y. 1954), *remanded*, 217 F. 2d 647 (2d Cir. 1954); *Harr* v. *Pioneer Mechanical Corp.*, 2 F. Supp. 517 (S. D. N. Y. 1932), *modified*, 65 F. 2d 332 (2d Cir. 1933), *cert. denied*, 290 U. S. 673 (1933).

Indeed, the foregoing principles and their consistent application by New York federal courts are based upon the simple proposition that a shareholder derives his status from the law of the place of incorporation and his rights vis-a-vis his corporation must therefore be determined by such law. *Rogers* v. *Guaranty Trust Co.*, 288 U. S. 123 (1933); *Canada Southern Ry.* v. *Gebhard*, 109 U. S. 527 (1883). And when the law of the place of incorporation, which created the status of the stockholder, conditions his right to sue on its behalf, such condition "will be observed elsewhere". See *Wood & Selick, Inc.* v. *Compagnie Generale Transatlantique*, 43 F. 2d 941, 942-43 (C. C. A. 2, 1930).

The "contacts" rule of *Auten* has never been applied by the New York courts to stockholder litigation and petitioners have shown no "developing line of authority" to that extent. Certainly, the *Auten* rule has not displaced in New York the "internal affairs" rule. Even petitioners concede that the *Auten* rule has been applied so far only in contract and tort litigation.[9]

Nor is the New York Business Corporation Law, §§ 1317-20, effective April 1, 1963, indicative of a trend in legislative, much less judicial, thinking with which the court below should have concerned itself. There is nothing in the record in this case to indicate that Pantepec is authorized to conduct or actually conducting business in New York with at least two-thirds of its outstanding stock or two-thirds of its voting stock owned by residents of the state, or with two-thirds of its business or investment income allocable to the state for franchise tax purposes.

Finally, New York public policy, as expressed in its decisions, is entirely consistent with the result below. Venezuelan law, although different from New York law, is neither fundamentally unfair nor unjust. Venezuelan law on the subject of shareholders' suits is substantially similar

[9] Petitioners' brief, p. 15.

to the law of Massachusetts. This similarity, whereby corporations are considered best suited to govern their own affairs, is illustrated by the opinion in *Pomerantz* v. *Clark*, 101 F. Supp. 341 (D. Mass. 1951) which, effectively, is summarized in the following finding of the trial court (23a).

> "31. The foregoing findings reflect the policy of the Venezuelan law to the effect that neither an individual stockholder nor the court is best fitted to determine whether it is to the interest of a Venezuelan business corporation to enforce corporate claims even if those claims are founded on plainly unlawful conduct participated in by corporate officers and directors; that only the stockholders' meeting may decide not only if the claims have merit but also if the collective corporate welfare is best promoted by suing upon them."

American investors in Pantepec are not deprived by the decision below of the substantial rights and remedies accorded to them as stockholders under Venezuelan law (21a-23a). These petitioners have chosen to ignore the law of their corporate domicile. Instead, they have sought to assert rights in this jurisdiction which the chartering country does not give them. They have had adequate opportunity to voice their contentions in the courts below and do not require another federal forum.

Conclusion

The petition for certiorari should be denied.

Respectfully submitted,

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Pantepec Oil Company, C. A.

Dated: May 4, 1962.

Office-Supreme Court, U.S.
FILED
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JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 805

NATHAN HAUSMAN, JOSEPH APPLEBAUM, THE APPLEBAUM FOUNDATION, INC., ALFRED N. BARNETT, JULIE A. BUCKLEY, as remaining trustee u w of Daniel Buckley, deceased, PETER FUNDARO, HAROLD MALTZ, NORVIN H. RIESER, FRED WEIBERT and REGINA WEIBERT and L. H. LUCKETT, in their own behalf as stockholders of Pantepec Oil Company, C.A., and in behalf of all other such stockholders similarly situated,

Petitioners,

—against—

JOHN W. BUCKLEY, THE CATAWBA CORPORATION and PANTEPEC OIL COMPANY, C.A.,

Respondents.

REPLY BRIEF OF PETITIONERS NATHAN HAUSMAN, *ET AL.*

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In the

Supreme Court of the United States

October Term, 1961

No. 805

Nathan Hausman, Joseph Applebaum, The Applebaum Foundation, Inc., Alfred N. Barnett, Julie A. Buckley, as remaining trustee u w of Daniel Buckley, deceased, Peter Fundaro, Harold Maltz, Norvin H. Rieser, Fred. Weibert and Regina Weibert and L. H. Luckett, in their own behalf as stockholders of Pantepec Oil Company, C.A., and in behalf of all other such stockholders similarly situated,

Petitioners,

—against—

John W. Buckley, The Catawba Corporation and Pantepec Oil Company, C.A.,

Respondents.

REPLY BRIEF OF PETITIONERS NATHAN HAUSMAN, *ET AL.*

The petition urges that certiorari be granted for the following reasons:

1. There is no state rule, "clearly enunciated" (App. A to pet., p. 37) or otherwise, of mechanical referral to the law of the state of incorporation.

2. Notwithstanding that the choice of law issue is of first impression and of far-reaching importance to Pantepec's thousands of American shareholders and to many other American investors in non-American corporations, the court

below explicitly refused to function in the manner of a state court of last resort and to pass upon the merits of the basic question of law before it.

3. The rationale of the decision below invites use of a foreign charter to plunder American investors and to evade the whole body of protective state and federal case and statute law.

4. In the nature of this type of controversy, the question at bar is far more likely to arise in diversity cases in the federal court than in New York or other state courts; and if not reviewed by this Court, it may be years before the rule applied below can be successfully challenged.

5. The decision below leaves thousands of American shareholders, in what is essentially an American enterprise, and untold others similarly situated, completely without any practical remedy.

Several of these points are wholly ignored in the answering briefs and not one of them is fairly met.

I

Newman v. *Baldwin*, 13 Misc. 2d 897, 179 N. Y. S. 2d 19 (Sup. Ct. N. Y. Co. 1958), is the respondents' prime authority, as it was of the court below. None of the respondents questions our submission (pet. pp. 10-11) that the *Newman* case has no force as a precedent in any of the state appellate courts, and that it is not binding on any of the numerous state justices of coordinate jurisdiction. The *Newman* case does *not* exemplify "rules of decision commonly accepted and acted upon by the bar and inferior courts" in New York, as suggested by Pantepec (br. p. 6) by quotation from *West* v. *American Telephone & Telegraph*

Co., 311 U.S. 223, 236 (1940). The *Newman* case stands completely alone, being the *only* state decision at any level on fulfillment of pre-conditions for maintaining a suit of this nature in behalf of a foreign corporation.* Petitioners urge that it is a matter of most serious concern that, in this federal diversity case, a ruling of such nature bars thousands of American shareholders from complaining of continuing self-dealing and overreaching by an American management.

For other New York "authority" the respondents perforce refer to various of the old dicta cited in the opinion below. It is easy to see why none of these additional citations is discussed by respondents. None of them even remotely touches on the present question.

Russian Reinsurance Co. v. *Stoddard*, 240 N. Y. 149, 147 N. E. 704 (1925), was an action by a foreign insurance company to recover its statutory deposit. *German-American Coffee Co.* v. *Diehl*, 216 N. Y. 57, 109 N. E. 875 (1915), was an action by a foreign corporation against its directors to recover illegally paid dividends. *Vanderpoel* v. *Gorman*, 140 N. Y. 563, 35 N. E. 932 (1894), was an action against a sheriff by an assignee for creditors of an insolvent corporation to recover assets attached despite the assignment. *Matter of American Fibre Chair Seat Corp.*, 265 N. Y. 416, 193 N. E. 253 (1934), was a statutory proceeding for confirmation of the election of a director of a New York corporation. In *Long Park, Inc.* v. *Trenton-New Brunswick Theatre Co.*, 297 N. Y. 174, 77 N. E. 2d 633 (1948), the validity of an agreement among shareholders of a foreign

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* *Hirshhorn* v. *Hirshhorn*, 280 App. Div. 791, 112 N. Y. S. 2d 841 (2d Dept. 1952), also presented such a question but did not decide it because of inadequate proof of the foreign law. A concurring opinion therein on the merits found local rather than foreign law to be applicable. See petition, page 10.

corporation was determined under local rather than foreign law, Pantepec's reliance (br. p. 8) being on the dissenting opinion. Even the dicta in these cases were of the most general character and in no way envisaged the present issue. Not one of these decisions, nor any cited in the opinion below, furthermore, involved a non-American corporation. And neither of the answering briefs has ventured to comment on the numerous New York cases cited at pages 16-17 of the petition holding that claims against directors, officers and third parties for mismanagement and fraud do not involve "internal affairs".

Nor, we believe, is support for the ruling below to be found in other federal decisions which do not deal with the question at bar and in any event can have no better foundation than the decision sought to be reviewed.

If the foregoing state decisions reflect a "clearly enunciated state rule" which justifies a United States Court of Appeals in refusing to pass upon the merits of the legal issue before it and in refraining from applying the rule that it thinks "better or wiser" (App. A to pet., p. 37), diversity litigants should hereafter resort to a federal court only with the greatest trepidation.

II

Buckley's brief (p. 8) disingenuously suggests a predominance of Venezuelan contacts by reference to Pantepec's business prior to the "Phillips Agreement" which is the subject of the discontinued first count. The overwhelming American contacts, summarized at pages 5-6 of the petition, are ignored in both respondents' briefs, as they are in the opinion below.

III

In the trial court the defendants established that the rights granted to minority shareholders by the Venezuelan Code are "futile" and "theoretical" (192a). The trial judge expressly stated that it was proven that petitioners have no remedy under the law of Venezuela (153a).

The antediluvian law of Venezuela, well-calculated to throttle minority shareholders (158a-159a), is summarized at pages 6-7 of the petition. It is not correct, as Buckley now asserts (br. p. 11), that any stockholder may place his complaint and the basis therefor before a stockholders' meeting. Plainly all complaints must be channeled through the "comisario" who, in the case of a corporation like Pantepec, is a hireling of management and may even be on the company payroll (188a [Art. 310]; 150a-151a; 154a-155a). The impossible deposit requirement, mentioned at page 7 of the petition and disputed by Buckley (br. p. 12), unquestionably is mandatory in the case of bearer shares like Pantepec's (157a, lines 10-12; 31a).

The claimed equation between the Venezuelan law and the "Massachusetts rule" (see *S. Solomont & Sons Trust, Inc.* v. *New England Theatres Operating Corp.*, 326 Mass. 99, 93 N. E. 2d 241 (1950); *Pomerantz* v. *Clark*, 101 F. Supp. 341 (D. Mass. 1951)) is specious because (1) in Venezuela only holders of 10% or more of stock have a right to lay a complaint before a shareholders' meeting, whereas in Massachusetts any shareholder may do so; (2) in Venezuela complaining shareholders have to deposit their shares until the conclusion of the shareholders' meeting, whereas no such requirement prevails in Massachusetts; (3) in Venezuela a majority vote against a suit is conclusive even though the wrongdoers control the shareholders' meeting, whereas in Massachusetts only the vote of a disinterested majority can bind the minority; and

(4) in Venezuela small shareholders of large companies have no practical means of mustering the 10% necessary to lay a complaint before the shareholders' meeting, access to the stock list being restricted to the fifteen days immediately in advance of the meeting, whereas no such obstacle obtains in Massachusetts. Furthermore, it is far from clear that New York would be bound to give effect even to the Massachusetts rule if the interests of New York citizens predominated over those of Massachusetts in one of its corporations. Cf. *Watson* v. *Employers Liability Assurance Corp.*, 348 U. S. 66 (1954); *Wells* v. *Simonds Abrasive Co.*, 345 U. S. 514 (1953); *Griffin* v. *McCoach*, 313 U. S. 498 (1941); Currie, *The Constitution and the Choice of Law*, 26 U. of Chi. L. Rev. 9 (1958). The basic philosophical difference between Massachusetts which has no faith in the prophylactic effect of minority stockholders' suits, and all the other states which find them useful, has been commented on at length by Judge Wyzanski in *Pomerantz* v. *Clark*, *supra*, 101 F. Supp. at pp. 346-7. New York is perhaps first among all the states in its readiness to cast off ritualistic conflict-of-laws rules subversive of its own interests and policy. *Kilberg* v. *Northeast Airlines, Inc.*, 9 N. Y. 2d 34, 172 N. E. 2d 526 (1961). Notwithstanding, petitioners have lost their day in court on the admittedly unreasoned assumption that New York would mechanically apply the anachronistic and iniquitous law, not even of a sister state, but of a foreign country having no conceivable interest in the controversy.

Dated, New York, N. Y.
May 5, 1962

Respectfully submitted,

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